

Weekly Market View

Three things to watch at Jackson Hole

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→ In this report, we highlight three potential catalysts to watch out for in Fed speeches that we believe are likely to set the tone for markets in the coming weeks and months.

What are the equity market implications of China's latest policy developments?

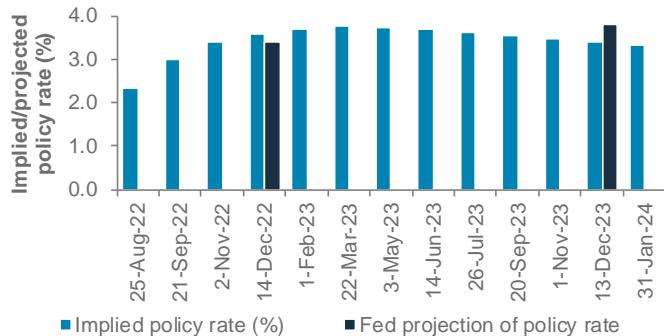
Could the US 10-year government bond yield test 3.5% again?

Is the USD likely to break into a 20-year high?

Charts of the week: Will the Fed unsettle markets?

Markets expect the Fed to end rate hikes by early 2023; USD, bond yields could extend rally if the Fed turns more hawkish

Money market estimate of Fed rate hikes and Fed's projections



Source: Bloomberg, Standard Chartered

US 10-year government bond yield, USD (DXY) index



Editorial

Three things to watch at Jackson Hole

All eyes are on the three-day annual Fed conference at Jackson Hole, with the focus particularly on Chair Powell's speech on 26 August. Markets are going into this potentially pivotal event with expectations of hawkish Fed commentary as central banks worldwide remain focussed on taming inflation running at multi-decade highs. The two-month-long equity rally has stalled, with the S&P500 pulling back from its key 200-day moving average resistance, the 10-year US Treasury yield rising above 3% for the first time since mid-July and the USD attempting to break out into a 20-year high.

At Jackson Hole, we will watch out for three potential catalysts in Fed speeches that we believe are likely to set the tone for markets in the coming weeks and months:

Consensus among Fed policymakers for another 75bps hike in September. Market expectations are split between a 50bps and 75bps hike next month following mixed data: the US job market remains red-hot (jobless rate is at a 50-year low), which continues to fuel wages, consumption and house rents. This week, durable goods orders data also suggested business spending remained healthy. However, policymakers will have to weigh that against a slump in business confidence (PMIs for August indicated a sharp contraction in US economic activity in Q3). Meanwhile, housing markets continue to weaken as this year's surge in mortgage rates starts to bite (July US house prices suffered their biggest m/m decline since 2011). *Markets are not expecting the Fed to waver in the face of weaker PMI and housing data amid a tight job market, but this implies that any signs the Fed is considering softening its stance – by slowing the pace of rate hikes, for example – would likely boost risk assets in the near term.*

Any rethink of the Fed's 2.5% neutral policy rate estimate. After a scorching pace of rate hikes this year (225bps in five months), the Fed's policy rate has risen to the estimated so-

called 'neutral' 2.5% rate, beyond which any further tightening should theoretically start to make financial conditions restrictive and slow growth. The Fed currently projects a policy rate of 3.4% by end-2022 and 3.8% by end-2023, before rate cuts bring it down to 3.4% by end-2024. However, the continued strength of the job market and consumption, despite the policy tightening thus far, has raised concerns that the neutral rate and terminal (or end-of-cycle) rate could be higher than the Fed's estimates. *Any hint that Fed policymakers are considering an upward revision of these key rate estimates would risk a significant shift in market expectations, a scenario that could potentially push the USD above its 20-year high and the 10-year US yield beyond its 3.5% June peak, causing a near-term pullback in risk assets.*

Any reassessment of the Fed's long-term 2% inflation target. While this is arguably the least likely of the three, it is possible the Fed may consider raising its inflation target on the grounds that structural inflation has risen after the pandemic, especially amid concerns that globalisation is reversing. US CPI inflation, running at a 40-year high above 8%, is likely to slow in the coming months due to base effects as well as easing commodity prices and supply bottlenecks. However, where inflation settles after peaking is more relevant, in our view. The Fed currently expects US core inflation (core PCE, one of the Fed's preferred measures) to end 2023 at 2.7% and 2024 at 2.3% (vs. 4.8% in June). Given its 2% inflation target, these projections suggest the Fed would have to continue tightening its policy far longer than the markets currently expect (ie, early 2023), even if that leads to a sharp slowdown in growth. *Any indication that Fed policymakers may be considering raising the inflation target to 2.5-3% is likely to ease investor concerns about an overly aggressive Fed policy in the coming months, a scenario that could cause the USD to pull back, the Treasury yield curve to steepen and global risk assets to rally.*

— Rajat Bhattacharya

The weekly macro balance sheet

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

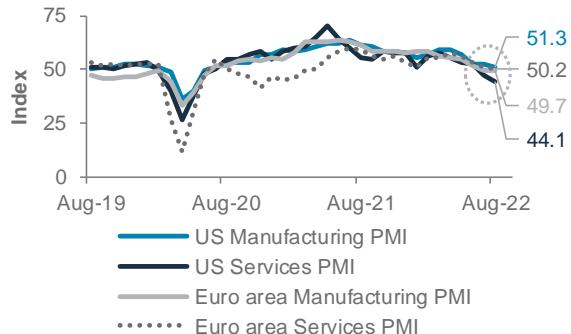
(+ factors: US durable goods orders, China rate cut, policy stimulus

(- factors: Weak US, Euro area PMI, US housing data

	Positive for risk assets	Negative for risk assets
COVID	<ul style="list-style-type: none"> China reopened to foreign students for the first time since COVID outbreak 	<ul style="list-style-type: none"> COVID-19 cases in China remained elevated
Our assessment: Neutral – Elevated case numbers in China vs reopening to foreign students		
Macro data	<ul style="list-style-type: none"> US core durable goods orders rose more than expected US jobless claims fell more than expected 	<ul style="list-style-type: none"> US manufacturing and services PMIs fell more than expected; services PMI reflected sharp contraction in activity US home sales fell more than expected; mortgage applications extended drop; house prices dropped the most m/m since 2011 Euro area services PMI fell more than expected, manufacturing PMI fell to contraction territory Euro area consumer confidence fell more than expected
Our assessment: Negative – Weak US, Euro area PMIs, US home sales vs strong US durable goods orders		
Policy developments	<ul style="list-style-type: none"> China cut five-year loan prime rate used for mortgage loans by more-than-expected 15bps China unveiled 19-point stimulus package President Biden cancelled USD10,000 in student loans for low-income borrowers 	
Our assessment: Positive – China rate cut, stimulus package		
Other developments	<ul style="list-style-type: none"> US sent Iran its final proposal to revive the 2015 nuclear pact 	<ul style="list-style-type: none"> Russia's Nord Stream 1 gas pipeline was shut for unscheduled maintenance
Our assessment: Neutral – Hopes of US-Iran nuclear deal vs Russian gas supply uncertainty		

US and Euro area business confidence continued to weaken in August

US and Euro area manufacturing and services PMIs



Source: Bloomberg; Standard Chartered

US home sales have sharply declined in recent months as high mortgage rates start to bite

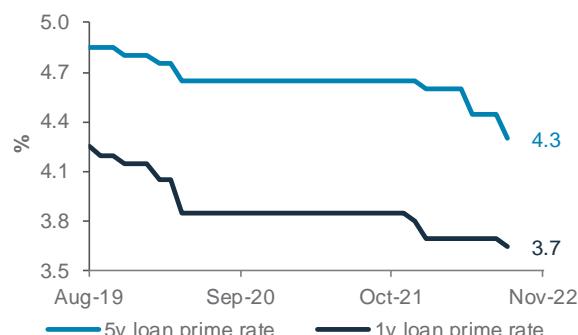
US new and pending home sales



Source: Bloomberg, Standard Chartered

China's central bank cut a key five-year lending rate used for mortgages and infrastructure loans in a bid to revive property sector lending

PBoC's 1y and 5y loan prime rates



Source: Bloomberg, Standard Chartered

Top client questions

Q Could the 10-year US government bond yield test 3.5% again?

In the short term, technicals argue the current upward trend could extend, resulting in a likely retest of interim resistance at 3.26%. Whether the yield turns lower from there or breaks higher to retest 3.50% is likely to depend on three factors.

The first is the Fed's tone. An unexpectedly hawkish tone either on inflation or in the form of an upward revision in the estimated 'neutral' rate at Jackson Hole, for example, would risk pushing the yield above 3.26%.

The second is US inflation data. Upside surprises in the PCE inflation data due on Friday, ISM prices paid and wage growth next week, and the August CPI release due in mid-September would risk triggering a retest of the 3.5% yield level.

Third, reports of rising short investor positioning raise the upside bias for bond yields, on the margin.

— **Manpreet Gill, Head, FICC strategy**

Q Is the USD likely to break into a new high?

The USD index (DXY) rebounded from key support around 105.70 in mid-August after a failed attempt to break sustainably below this level. This rebound was accompanied by (i) a rise in US government bond yields as Fed policymakers emphasised that the fight with inflation was not over and (ii) continued downward pressure on the EUR (a large weight in the DXY) following worries of a sharp downturn in growth in the region.

The USD faces key technical resistance at the recent high around 109.3. A hawkish message from the Fed at Jackson Hole over the weekend (including any hint of upward revisions in what is considered the 'neutral' rate) may be needed to push the USD above this threshold. This scenario reinforces the near-term bullish USD trend and brings 111.3 into focus. EUR/USD is likely to weaken in this scenario, with 0.990 and 0.985 as key supports. Without a hawkish Fed as a catalyst, the DXY is likely to fall back within its 105.3-109.3 range for now.

— **Manpreet Gill, Head, FICC strategy**

US CPI inflation eased sharply in July; a sustained decline in inflation would enable the Fed to ease the pace of rate hikes, pulling bond yields lower

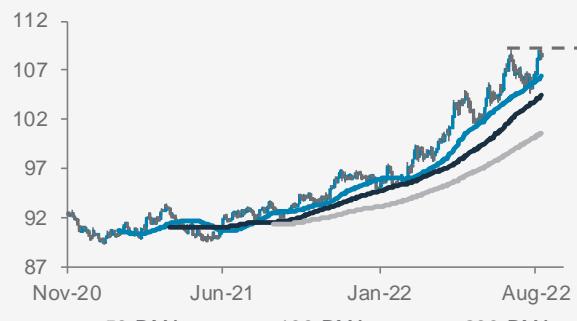
US CPI inflation m/m



Source: Bloomberg, Standard Chartered

Any hawkish Fed commentary at Jackson Hole could push the USD index to break out into a 20-year high above 109.3

USD index (DXY)



Source: Bloomberg, Standard Chartered

Top client questions (cont'd)

Q What are the equity market implications of China's latest policy developments?

Chinese equities have recently underperformed global equities amid a weak Q2 22 earnings season. About 1/8th of the companies in MSCI China index and 1/3rd of companies in MSCI China A onshore index missed consensus earnings expectations. Chinese property markets also remain under pressure amid liquidity pressure on developers.

However, we expect policies to remain supportive. For the real estate sector, the announcement of CNY 200bn of special bank loans and state-owned company guarantee for onshore bond issuance by qualified private developers are positives. More broadly, we also expect (i) further cuts in short-term rates and the loan prime rate (LPR), (ii) further relaxation of real estate purchase restrictions and down payment requirements for second homes, and (iii) more measures to support funding for selected projects/developers.

Moreover, earnings in the internet sector beat expectations amid disciplined cost control and measures to improve operational efficiency. We believe there is further room for this sector to rebound, especially if regulators in China allow US authorities to inspect the audit paperwork of US-listed Chinese companies in Hong Kong. We view the communication services sector, which comprises mostly of China internet consumption companies, as preferred.

— Daniel Lam, Head, Equity Strategy

Q What is the outlook for Japan equities?

Japan equities have underperformed global equities over the past year when measured in common currency USD terms (-17.7% vs -12.2%). While Japan equities have done better than global equities in local currency terms, JPY weakness more than offset this for global investors.

JPY's weakness has helped make product pricing more competitive for exporters and has boosted foreign earnings when translated into JPY. However, such benefits are lost to an investor outside Japan because of the fall in the JPY.

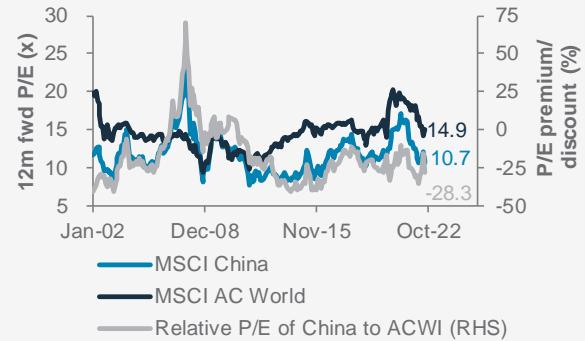
The likely forex impact notwithstanding, we see Japan equities as attractively valued at 13x consensus 12-month forward earnings, which is at the bottom end of its historical range, and a 13% discount to global equities. Earnings are being revised up following a healthy Q2 season, partly helped by the weaker JPY. Meanwhile, Japan's monetary policy continues to be supportive. Having said that, Japan continues to struggle with high COVID-19 cases which, together with rising cost of living, could hold back consumption. Japan's export orientation is also vulnerable to a global growth slowdown and investors are still wary of the Kishida administration's policies.

Overall, we see the risks as balanced and expect Japan equities to perform in line with global equities over the next 12 months.

— Fook Hien Yap, Senior Investment Strategist

China's equities are trading at a nearly 30% discount to global equities

12-month forward P/E for MSCI China and MSCI All-Country World indices and their P/E premium/discount



Source: Bloomberg, Standard Chartered

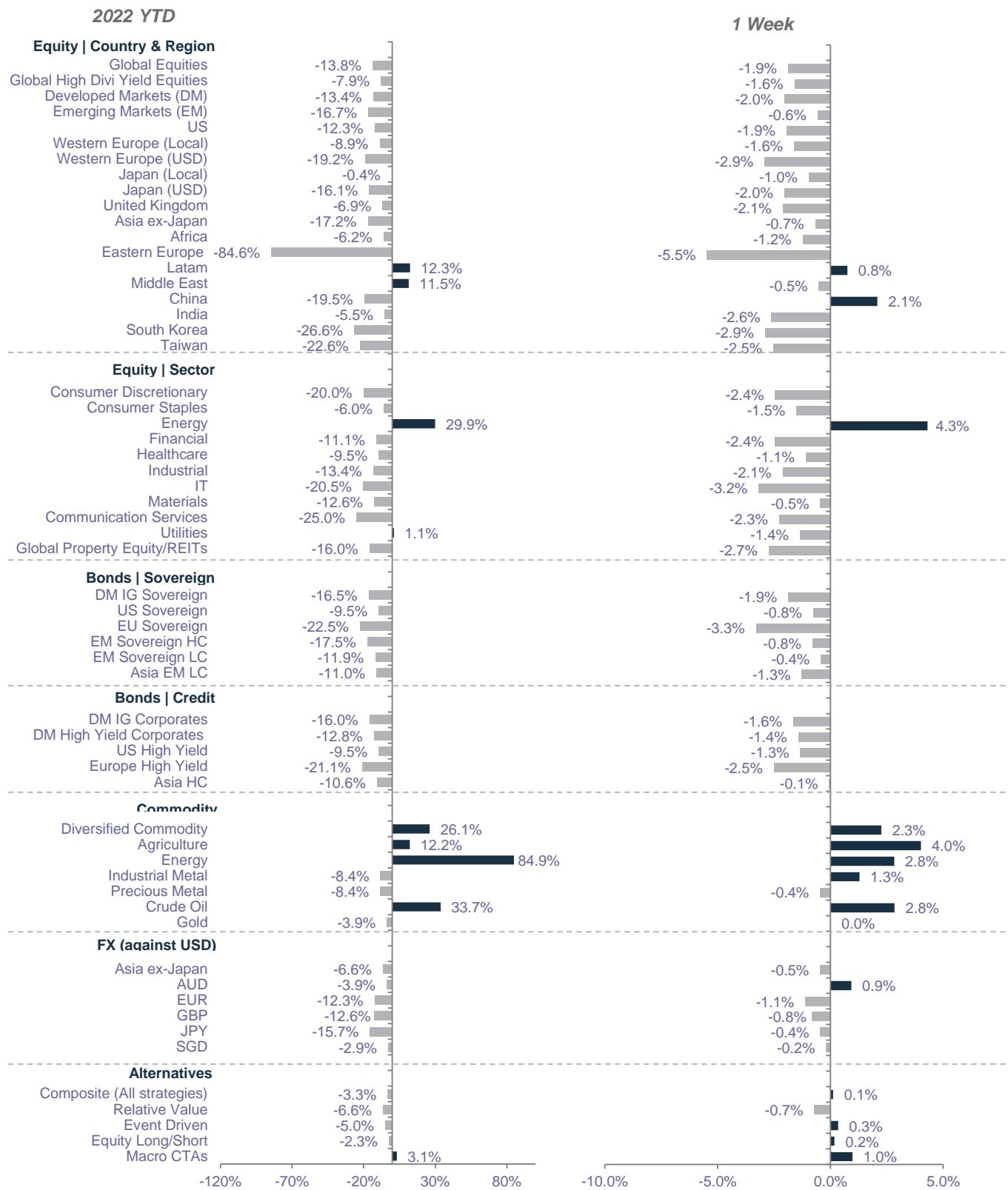
Japan equities outperformed global equities over the past year when measured in JPY, but underperformed global equities' performance in USD terms

12-month performance of MSCI Japan in JPY and USD and MSCI AC World in USD



Source: MSCI, FactSet, 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, 2022 YTD performance from 31 December 2021 to 25 August 2022; 1-week period: 18 August 2022 to 25 August 2022

Our 12-month asset class views at a glance

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

Source: Standard Chartered Global Investment Committee

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

Next resistance for the US 10-year bond yield is at 3.1%

Technical indicators for key markets as on 25 August

Index	Spot	1st support	1st resistance
S&P 500	4,199	4,142	4,242
STOXX 50	3,675	3,641	3,719
FTSE 100	7,480	7,451	7,530
Nikkei 225	28,479	28,218	28,835
Shanghai Comp	3,246	3,215	3,278
Hang Seng	19,968	19,502	20,202
MSCI Asia ex-Japan	642	633	647
MSCI EM	1,003	991	1,010
Brent (ICE)	99.3	96.8	101.5
Gold	1,757	1,742	1,765
UST 10y Yield	3.03	2.96	3.10

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

Economic and market calendar

	Event	Next week	Period	Expected	Prior
MON					
TUE	EC	Economic Confidence	Aug		– 99.0
	US	Conf. Board Consumer Confidence	Aug	97.5	95.7
	US	JOLTS Job Openings	Jul	10300k	10698k
WED	CH	Manufacturing PMI	Aug	49.5	49.0
	CH	Non-manufacturing PMI	Aug	52.6	53.8
	EC	CPI Estimate y/y	Aug		– 8.9%
THUR	CH	Caixin China PMI Mfg	Aug	50.1	50.4
	EC	Unemployment Rate	Jul		– 6.6%
	US	Unit Labour Costs	2Q F	10.8%	10.8%
	US	ISM Manufacturing	Aug	52.2	52.8
FRI/SAT	EC	PPI y/y	Jul		– 35.8%
	US	Change in Nonfarm Payrolls	Aug	295k	528k

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

Investor diversity remains reasonably high across assets

Our proprietary market diversity indicators as of 25 August

Level 1	Diversity	1-month trend	Fractal dimension
Global Bonds	●	→	1.40
Global Equities	●	→	2.11
Gold	●	→	1.46
Equity			
MSCI US	●	↑	1.70
MSCI Europe	●	↑	1.48
MSCI AC AXJ	●	↑	1.89
Fixed Income			
DM Corp Bond	●	↑	1.49
DM High Yield	●	↑	1.63
EM USD	●	↑	1.70
EM Local	●	↑	1.54
Asia USD	●	↑	1.46
Currencies			
Crude oil	●	↓	1.46

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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