Wealth Management Chief Investment Office
7 October 2022

Weekly Market View

Too soon for a Fed pivot

→ We believe it is to too premature to expect a central bank policy pivot. Markets were hoping that a peak in rates was near following weaker-than-expected US manufacturing and job openings data and a less hawkish RBA rate hike.

→ However, those hopes – and we shall call it 'hopes' at this stage – were dashed by a stream of central bankers from the US, Europe, Canada and New Zealand reiterating the need to continue with policy tightening until inflation falls closer towards their targets.

→ Against this backdrop, any near-term run-up in stocks is likely to be another bear market rally fuelled by oversold conditions, just like in July-August. We believe those over-exposed to equities or other risky assets should look to use any near-term rallies to rebalance away into Investment Grade corporate bonds in Asia and Developed Markets, which are paying the highest yields in a decade.

How do idiosyncratic risks affect your preferred view on the European financial sector?

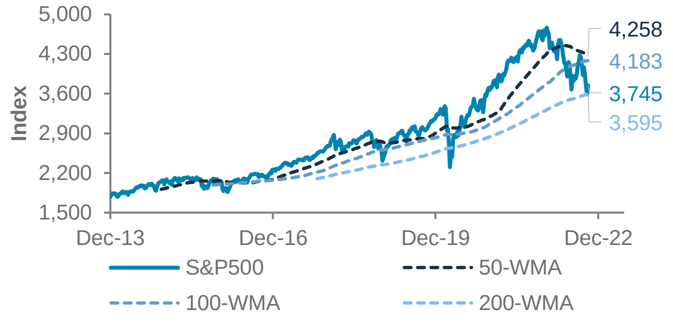
Are you still constructive on the AUD after this week's less hawkish RBA policy?

What is the outlook for oil after this week's surprising output cut decision from OPEC+?

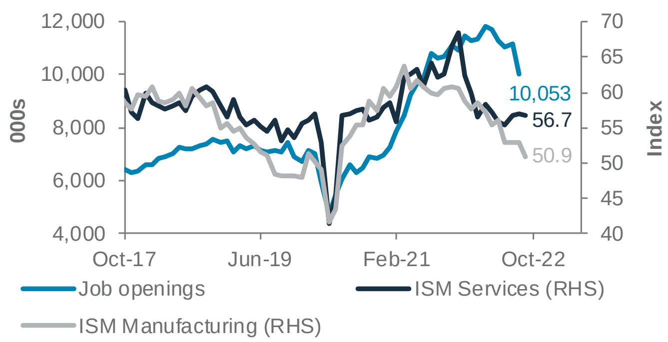
Charts of the week: Strong technicals, weak fundamentals

Stocks could see another rally from oversold levels, but fundamentals suggest the bear market is not over yet

S&P500 index, with 50-, 100- and 200-week moving averages



US JOLTS job openings, ISM Manufacturing & Services PMIs



Source: Bloomberg, Standard Chartered

Editorial

Too soon for a Fed pivot

We believe it is to too premature to expect a central bank policy pivot. Markets were hoping that a peak in rates was near following weaker-than-expected US manufacturing and job openings data and a less hawkish RBA rate hike. This explains the sharp rebound in stocks and bonds in the first couple of days of the week from oversold levels, following September's rout. However, those hopes – and we shall call it 'hopes' at this stage – were dashed by a stream of central bankers from the US, Europe, Canada and New Zealand reiterating the need to continue with policy tightening until inflation falls closer towards their targets. As a result, equities pared back the gains in the past couple of days. Money markets now expect Fed rates to rise another 150bps and peak at around 4.75% by March next year, compared with around 4.5% priced in at the start of the week, and ECB rates to peak at around 3% by July next year.

We believe job markets remain too tight both in the US and Europe and core inflation pressures too high for the central banks to relent anytime soon. In the US, for instance, job openings data (JOLTS) showed the labour market is cooling from near-record tight levels but it remains hotter than the Fed would like it to be and what is needed to bring down core inflation towards its 2% goal. Tonight's US non-farm payrolls data, which according to consensus is expected to show 255,000 jobs were created last month, underlines the tight market. The US unemployment rate is likely to stay at or below the current level of 3.7% (just above the 50-year low of 3.5% hit in July) as long as monthly job creation continues above 79,000, according to the Atlanta Fed's calculations (assuming stable labour participation). We believe the Fed will continue to raise rates until the jobless rate rises well above the long-term 4% target. In the Fed's latest forecasts, policymakers projected the unemployment rate to rise to 4.4% by Q4 next year.

Meanwhile, ISM data showed the US services sector remains strong, picking up the slack from the manufacturing sector as demand shifts from goods to services. This shift, in our view, is likely to keep services sector and core inflation elevated.

OPEC's decision this week to cut oil output by 2mbpd is likely to keep crude oil prices elevated. Meanwhile, Russia's annexation of four Ukraine regions and EU plans to cap Russian oil prices are likely to increase tensions in Europe, keeping energy prices elevated. There is also the risk of further escalation in US-Russia tensions ahead of the US mid-term elections where Democrats are slated to lose their majority in the Congress. No surprises then that a stream of Fed policymakers and ECB President Lagarde were all singing from the same hymn sheet this week – warning that rates need to go up higher and stay there for some time to bring down inflation.

Against this backdrop, any near-term run-up in stocks is likely to be another bear market rally fuelled by oversold conditions, just like in July-August. The S&P500, having rebounded from its 200-week moving average, faces key resistance around 3900, followed by 4100. The US 10-year government bond yield is also likely to retest September's 12-year high of 4%, especially if tonight's jobs data and inflation data on 13 October (the consensus estimates core CPI decelerated to 0.4% m/m in September) beat expectations. An underwhelming payrolls report and/or downbeat inflation data would of course provide a short-term relief rally in stocks and bonds.

Given this, we believe those over-exposed to equities or other risky assets such as High Yield bonds should look to use any near-term rallies to rebalance away into Investment Grade corporate bonds in Asia and Developed Markets, which are paying the highest yields in a decade. They could also consider averaging into deeply undervalued Asia ex-Japan and UK equities. We expect further policy easing in China once the Party Congress (starting on 16 Oct) is over. These measures should boost depressed local equities. Meanwhile, the global energy sector remains our top pick among equity sectors. We believe the sector offers an attractive way to hedge against a sustained inflationary scenario. OPEC's larger-than-expected output cut plan and a further drawdown in US inventories should keep oil prices elevated, supporting this equity sector.

— Rajat Bhattacharya

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: Slowing US job openings and manufacturing PMI

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

	Positive for risk assets	Negative for risk assets
COVID-19		• China's traditional Golden Week travel subdued due to COVID-19 restrictions • China banned residents from leaving Xinjiang after a COVID-19 outbreak
	Our assessment: Negative – Golden Week travel curbs	
Macro data	• Weaker-than-expected US ISM Manufacturing PMI, new orders PMI and JOLTS job openings	• Stronger-than-expected US ISM Services PMI • Euro area retail sales fell more than expected and producer price inflation rose more than expected • Germany forecast a 2023 recession and 8% inflation • China's non-manufacturing PMI fell below estimates
	Our assessment: Negative – In an environment when 'good news is bad news', the strong US services data, on balance, raises the odds of continued Fed policy tightening; China's weak non-manufacturing PMI; Europe's retail sales slump	
Policy developments	• RBA hiked rates by 25bps vs market expectations of a 50bps hike • UK Chancellor Kwarteng reversed plans to cut the top tax rate of 45% and brought forward the publication of his plan to cut UK's debt	• A stream of Fed officials reminded the need to continue raising rates and keeping it there until inflation falls closer to 2% • ECB minutes showed broad support for a 75bps hike this month • RBNZ hiked rates by 50bps as expected
	Our assessment: Negative – Hawkish Fed speeches	
Other developments		• OPEC+ cut output target by 2mbpd, tightening supplies • EU finalised plans to cap Russian oil prices
	Our assessment: Negative – OPEC output cut, escalation of Russia vs US/Europe tensions	

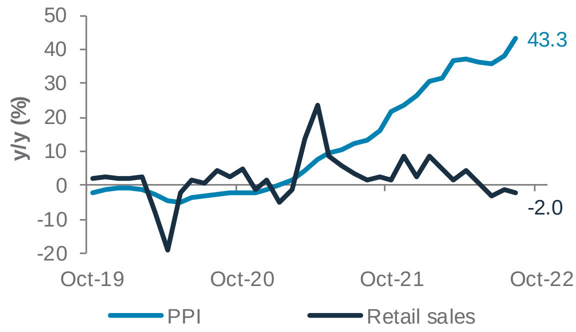
The US manufacturing sector appears to be slowing sharply as goods demand fades

US ISM PMI sub-indices for prices paid, new orders and employment

Source: Bloomberg; Standard Chartered

The Euro area faces rising stagflation pressures, with prices accelerating and demand contracting

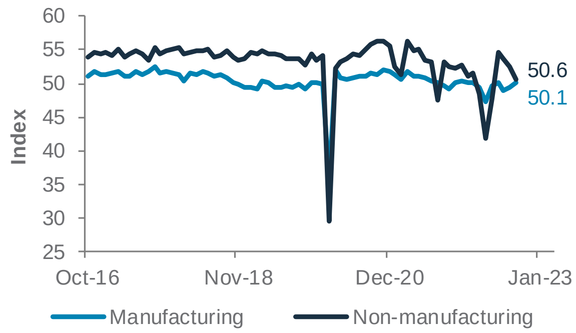
Euro area producer price inflation and retail sales



Source: Bloomberg, Standard Chartered

China's activity indicators remain lacklustre but we expect them to pick up as policy eases further after this month's Communist Party Congress

China's Manufacturing and Non-Manufacturing PMIs



Source: Bloomberg, Standard Chartered

Top client questions

How would idiosyncratic risks affect your preferred view on the European financial sector?

In recent weeks, negative headlines surrounding Credit Suisse drove poor sentiment for the financial sector. Concurrently, global equities made new 52-week lows in September and FX markets (particularly the GBP) saw extreme volatility. This backdrop and a continued tightening of financial conditions mean equity market volatility is likely to be elevated. However, we believe European banks are better capitalised than in previous cycles, offering a much stronger stability buffer for the financial system. The banking sector withstood the COVID-19-led recession and the Ukraine war well, and we expect it can also weather idiosyncratic risks. In our view, European financial equities remain attractively valued, at a time when higher interest rates should be supporting a sector re-rating. We expect the sector to outperform the broader market over 12 months. Near-term weakness offers an opportunity to add exposure for longer-term investors, even if further lows cannot be ruled out in the short term.

From a bondholder perspective, we remain constructive on the European banks' subordinated bonds sub-asset class, given adequate capital levels and expectations that banks would likely first stop equity dividends to preserve capital, if required (as experienced in 2020). Thus, we believe market concerns may be overdone. Hence, while near-term weakness cannot be ruled out, we view the yields and risk-reward as attractive for long-term investors.

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

European financial equities have declined c.8% in EUR terms along with the broader market in the past year; European banks' subordinated bonds are pricing in a significantly negative outlook

Total return of Bloomberg European subordinated bonds (CoCo* Tier 1, EUR hedged), MSCI Europe and MSCI Europe Financial equity indices

Source: Bloomberg, Standard Chartered
*See page 8 for explanatory notes on CoCo bonds

Do you expect the 10-year US Treasury yield to go higher?

This week, the benchmark 10-year US government bond yield fell on rising expectation of the Fed pausing its rate hiking cycle. While the weak September ISM manufacturing and job opening readings and weaker housing market data have fanned expectations, we believe a Fed "pivot" does not look likely yet. Firstly, the US job market remains strong, providing grounds for the Fed to stay the course with monetary policy tightening. Also, recent speeches by Fed policymakers reaffirmed the Fed's commitment to fight inflation. Lastly, although Australia's central bank did surprise with a smaller-than-expected rate hike, most global central banks retain a tightening bias, with the latest one being the RBNZ. Together, these factors lead us to believe that the bond yield risk is skewed to the upside. Hence, we retain our view that 10-year US Treasury yield could test 4% by the end of this year.

Given the recent softening of bond yields generally, we would use the window to reduce our exposure to Developed Market (DM) government bonds and look for opportunities to add to DM Investment Grade corporate bonds or Asia USD bonds, our preferred areas with bonds.

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

The US 10-year government bond yield could retest 4% towards end of this year

10-year US Treasury yield

Source: Bloomberg, Standard Chartered

Top client questions (cont'd)

Are you still constructive on AUD/USD after this week's less hawkish RBA policy?

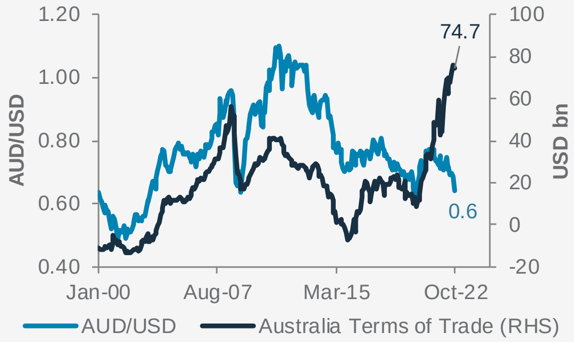
The RBA surprised the markets earlier this week, hiking policy rates by 25bps vs consensus expectation of 50bps. The RBA signalled it is still likely to continue hiking rates, albeit at a slower pace than before. This would provide it the opportunity to assess the impact of the rate hikes so far, given that typically the impact gets felt on the economy with a lag. Signs of weakness in the real estate market may also have been a consideration, given the majority of mortgage loans in Australia have variable rates.

A less hawkish RBA is likely to pose a headwind for AUD/USD in the near term, as 2-year relative real (net-of-inflation) yields are likely to turn less supportive than before. We see strong technical support in the 0.6330-0.6360 region. However, on a 12-month horizon, we see three supportive drivers which should push AUD/USD towards the 0.67-0.68 region: a. the currency pair's underperformance vs the terms of trade; b. relatively stronger Australian growth; and c. AUD undervaluation as supportive drivers.

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

We expect AUD/USD to move higher to catch-up with Australia's strong Terms of Trade

AUD/USD and Australia's Terms of Trade



Source: Bloomberg, Standard Chartered

What is the outlook for oil prices after this week's surprise decision from OPEC+?

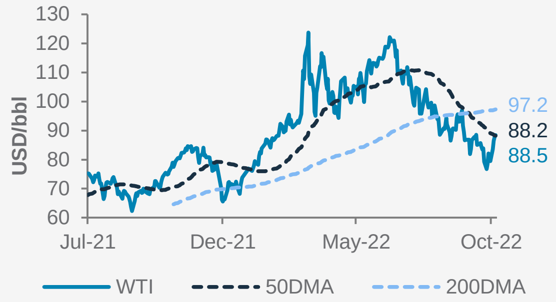
OPEC+ surprised markets with a relatively large output cut of 2mbpd, starting in November, with producers arguing the move was necessary to protect the industry and their own economies from slowing global growth. This was the largest output cut since the pandemic in 2020. The actual cut to output is likely to be smaller than this given the producers were struggling to meet prior output targets (with Saudi Arabia's energy minister estimating the actual cut at 1-1.1mn bpd), but the size is nevertheless significant.

We believe this action is consistent with our expectation that oil prices remain well-supported over the next 1-3 months, despite longer-term (6-12 month) risks to the downside. The OPEC+ cut, together with the upcoming imposition of sanctions and price caps on Russian oil exports, means the focus is likely to remain on supply risks over the next few months, though the US's decision to signal another Strategic Petroleum Reserve release could add some additional price volatility around this. From a technical standpoint, a WTI oil price break above 50-DMA (just above USD 88 currently) would make a rise towards USD 90, followed by the 200-DMA at USD 97, more likely in the near term.

— **Manpreet Gill,** *Chief Investment Officer, AMEE*

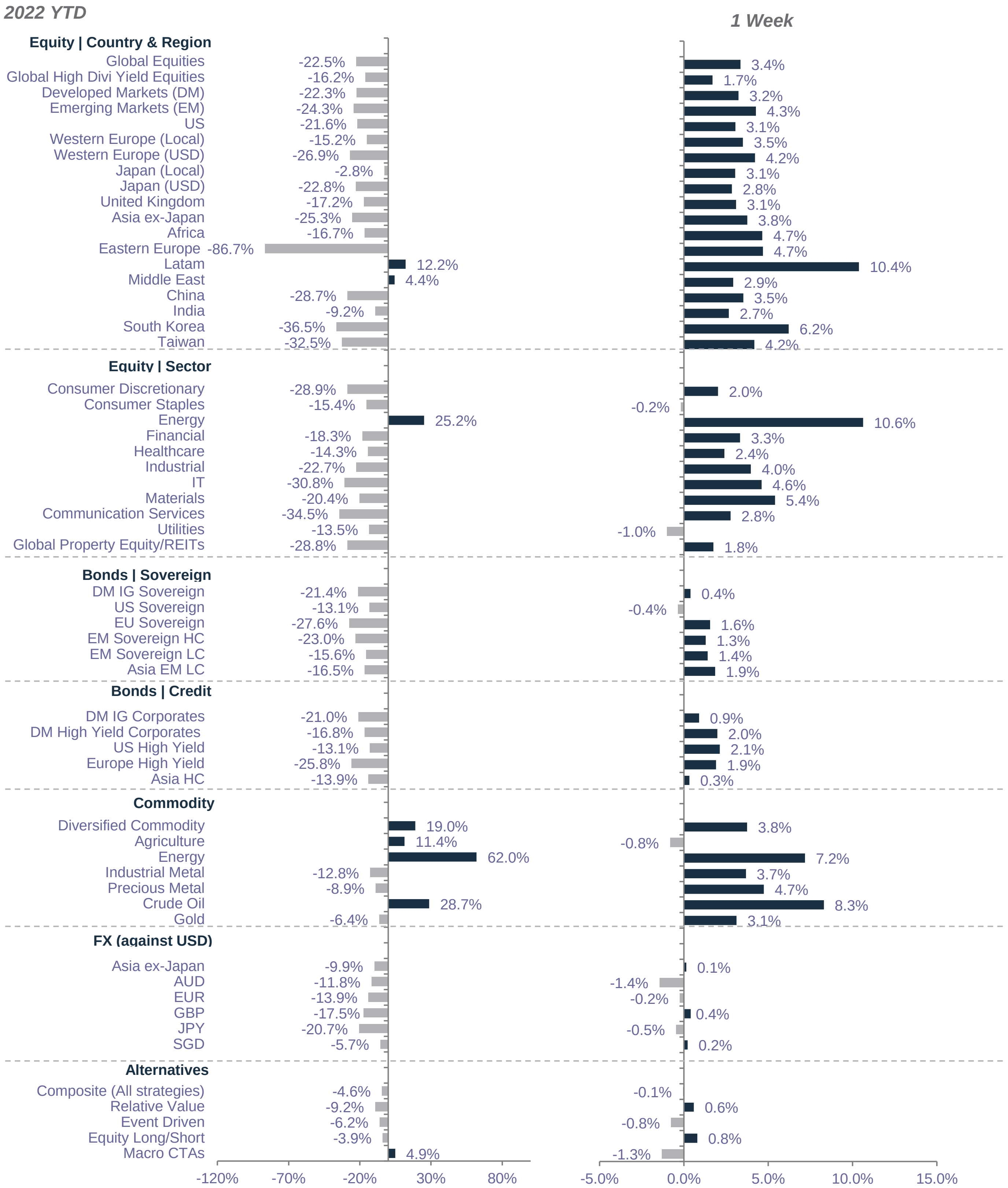
Crude oil faces near-term resistance around USD88/bbl; a break higher would target USD 90, followed by USD 97

WTI crude oil price



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, 2022 YTD performance from 31 December 2021 to 06 October 2022; 1-week period: 29 September 2022 to 06 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	EC	Sentix Investor Confidence	Oct	–	-31.8
TUE					
WED	US	PPI Ex Food and Energy y/y	Sep	7.3%	7.3%
THUR	US	CPI Ex Food and Energy y/y	Sep	6.5%	6.3%
FRI/SAT	CH	PPI y/y	Sep	1.1%	2.3%
	CH	CPI y/y	Sep	2.8%	2.5%
	US	Retail Sales Ex Auto and Gas	Sep	–	0.3%
	US	U. of Mich. Sentiment	Oct P	59.0	58.6
	US	U. of Mich. 1 Yr Inflation	Oct P	–	4.7%
	US	U. of Mich. 5-10 Yr Inflation	Oct P	–	2.7%
	CH	Exports y/y	Sep	4.0%	7.1%

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 resistance for the US 10-year bond yield is at 3.89%

Technical indicators for key markets as on 06 October

Index	Spot	1st support	1st resistance
S&P 500	3,745	3,623	3,828
STOXX 50	3,433	3,340	3,506
FTSE 100	6,997	6,899	7,091
Nikkei 225	27,060	26,228	27,602
Shanghai Comp	3,024	3,024	3,024
Hang Seng	18,012	17,365	18,374
MSCI Asia ex-Japan	578	561	586
MSCI EM	911	887	922
Brent (ICE)	94.5	90.1	96.6
Gold	1,710	1,672	1,737
UST 10y Yield	3.83	3.70	3.89

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 06 October

Level 1	Diversity	1-month trend	Fractal dimension
Global Bonds	◐	→	1.38
Global Equities	●	→	1.51
Gold	◐	→	1.34
Equity			
MSCI US	●	↑	1.74
MSCI Europe	◐	↓	1.36
MSCI AC AXJ	◐	↓	1.27
Fixed Income			
DM Corp Bond	◐	→	1.45
DM High Yield	●	↓	1.67
EM USD	●	↓	1.59
EM Local	◐	↓	1.42
Asia USD	◐	↓	1.50
Commodities			
WTI Crude Oil	◐	→	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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