



# Weekly Market View

## Tug of war

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→ Technical indicators, particularly for some markets such as China, suggest equities are heavily oversold and due for a technical bounce. However, we believe any rebound is likely to be another short-term bear market rally, unless Fed rate expectations and bond yields peak

→ We see better value in income assets that offer the highest yields in over a decade. Our multi-asset income allocation basket for investors with a moderate risk profile now yields around 7%

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What are the investor implications following China's recent policy developments?

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What can we learn from the US earnings season so far?

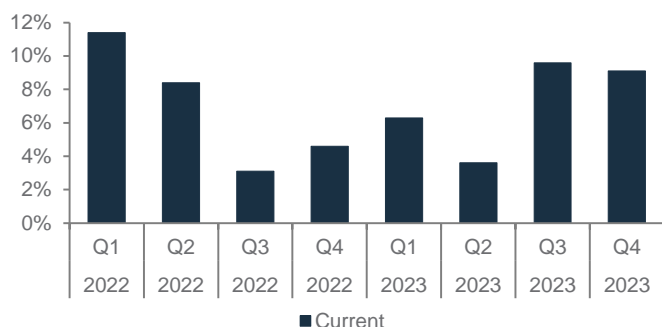
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Do you expect the JPY and GBP to bottom soon?

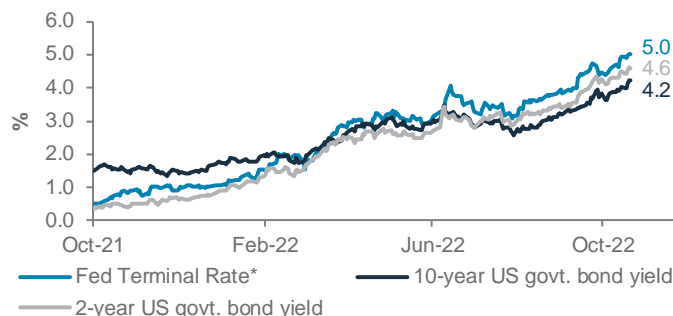
## Charts of the week: Earnings collide with rising bond yields

**US companies have beaten Q3 earnings estimates so far, but rising bond yields remain headwind to stocks**

US S&P500 actual earnings (Q1 22) and consensus estimates



US 2- and 10-year government bond yields, Fed terminal rate\*



Source: Bloomberg, Standard Chartered; \*Market expectations of the Fed terminal rate, assuming Fed rate peaks in May 2023

## Editorial

### Tug of war

Market moves this week reflect the ongoing tussle between the still robust US economic growth, as seen in corporate earnings beats so far, and rising bond yields. Thanks to the earnings performance, global stocks rebounded from a key support level, which has been tested thrice over the past three weeks. Technical indicators, particularly for some markets such as China, suggest equities are heavily oversold and due for a technical bounce. However, we believe any rebound is likely to be another short-term bear market rally, unless Fed rate expectations and bond yields peak. We see better value in income assets that offer the highest yields in over a decade.

Almost a fifth of US S&P500 index members have reported earnings so far, of which 75% have beaten consensus estimates, above the long-term average of 66%. Although part of the beats was because companies guided estimates lower ahead of the earnings season, the results show some businesses, especially in energy and industrial sectors, continued to benefit from strong pricing power i.e., they could pass on higher operating costs to consumers. The Q3 earnings are corroborated by macroeconomic data. The Atlanta Fed's GDPNow estimated US GDP rebounded to a 2.9% annualised rate in Q3, from a -0.6% contraction in Q2.

However, underneath these headline numbers, we see growing challenges to corporate earnings. For one, earnings in Q3 (and this year) have been propped up by stellar energy sector profits because of the surge in oil prices. While this factor supports our preference for the energy equity sector globally, excluding the energy sector, US Q3 earnings likely fell 3.6%, according to Refinitiv. Moreover, rising wage pressures and borrowing costs are likely to hurt profit margins in the coming quarters. As margins are squeezed, companies typically cut investments, hurting future profits. Thus, we see risk of further downgrades to earnings estimates in the coming year (see chart & page 5).

Meanwhile, the continued surge in bond yields raises the risk of further derating of equities. The US 10-year and 2-year government bonds yields have already shot past our upgraded 3-month estimates of 4% and 4.5% made only a month ago. While we expected temporary overshoots in the near-term, the main drivers of bond yields have been the surprisingly strong consumer inflation and job market data for September. Markets now expect the Fed's key rate to peak close to 5% in May 2023, compared with c. 4.5% estimated only a month ago. Higher bond yields raise the discount rate used to generate the present value of equities. This is a major factor which dragged US 12-month forward equity P/E ratio from above 20 at the start of the year to below 16. Thus, we believe the bar for a sustained rebound in equities is high until bond yields peak. Charts suggest the S&P500 needs to decisively break above 3,800 for a sustained uptrend, with the next major resistance near 4,100.

Instead, we see much better opportunities for investors in income-generating strategies, including high grade corporate bonds. Our multi-asset income allocation basket for investors with a moderate risk profile now yields around 7%. Through this basket, investors can lock in decade-high yields from Developed Market Investment Grade corporate bonds (yielding 5.8%) and Asia USD-denominated corporate bonds (yielding 8%). The latter is overwhelmingly composed of Investment Grade bonds. Just over a quarter of the income basket is made of high dividend paying equities, which have historically been more resilient than the broader equities during recessions.

**What we are watching:** (1) China's new leadership line-up post the Party Congress to signal policy direction (see page 5); (2) ECB meeting, where rates are likely to rise by 75bps, and President Lagarde's resolve to continue with rate hikes in the face of a likely recession; (3) Business confidence indicators (PMIs) likely to signal deepening contractions in Europe; and (4) UK leadership race for the next Conservative PM.

## 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:** UK U-turn on budget, recovering Michigan cons. sentiment

**(-) factors:** Weak US retail, BoE to start QT, China sticks with policy

	Positive for risk assets	Negative for risk assets
COVID-19		<ul style="list-style-type: none"> <li>China's Xi defended Zero-COVID policy in his Congress speech</li> <li>Hong Kong Chief Executive John did not offer specifics on pandemic curbs in his maiden policy address</li> </ul>
	<b>Our assessment: Negative</b> – Near-term easing of COVID-19 curbs in China and Hong Kong appears unlikely	
Macro data	<ul style="list-style-type: none"> <li>Michigan consumer sentiment higher than consensus</li> <li>Euro area ZEW survey on growth expectations was better than expected</li> <li>Euro area CPI accelerated less than expected to 9.9%; core inflation matched expectations (4.8%)</li> </ul>	<ul style="list-style-type: none"> <li>US retail sales stagnated, missing expectations</li> <li>New York Fed Mfg dropped more than expected</li> <li>US NAHB housing market index fell close to COVID-19 lows; housing starts were lower than expected</li> <li>Uni. Of Michigan inflation expectations ticked up</li> <li>UK core and headline CPI higher than expected</li> </ul>
	<b>Our assessment: Negative</b> – Weak US retail sales and housing starts, rising US inflation expectations	
Policy developments	<ul style="list-style-type: none"> <li>UK scrapped most of its mini-budget proposals and signalled more cost saving measures, including a windfall tax on companies; PM Truss's resignation raises scope of further market-friendly policies</li> </ul>	<ul style="list-style-type: none"> <li>BoE ended bond purchases and announced QT to start in November</li> <li>President Xi signalled no change in economic policy; China kept 1-year lending rate constant</li> <li>Fed speakers stay hawkish</li> </ul>
	<b>Our assessment: Negative</b> – BoE to start QT, China maintained policy	
Other developments	<ul style="list-style-type: none"> <li>Reports of US releasing more strategic oil reserves</li> </ul>	<ul style="list-style-type: none"> <li>Russia continued to bomb Kiev, Ukraine power plants</li> </ul>
	<b>Our assessment: Neutral</b> – US oil reserve release vs escalation in Russian attack on Ukraine	

**Our 'Fear and Greed' index is near the same level from where the last bear-market rally started in June**

Our Fear & Greed indicator\*



Source: Bloomberg; Standard Chartered; \*Takes into account market momentum, equity strength, market breadth, equity vs bonds, market volatility and put-call ratio

**Downside pressure on the US housing market is increasing as long-term interest rates rise**

US housing starts and building permits



Source: Bloomberg, Standard Chartered

**Euro area growth expectations continued to decline, which signals further downside for economic activity going forward**

Euro area ZEW survey of growth expectations minus current conditions vs Euro area PMI



Source: Bloomberg, Standard Chartered



## Top client questions

### Q What are the investor implications following China's recent policy developments?

The long-awaited 20<sup>th</sup> Congress of the Chinese Communist Party started on 16<sup>th</sup> October and is expected to end on 22<sup>nd</sup> October, following which the new leadership line-up of the ruling Communist Party will be unveiled. Here, we summarise a few key points from President Xi's keynote speech that we see as pertinent for investors: 1) China's Dynamic Zero-COVID strategy is unlikely to come to a sudden end; 2) Common prosperity remains high on the priority list; 3) Self-reliance in key technology areas remains a critical driving force of economic development; 4) Economic growth is still the party's top priority, together with national security; 5) Work is in progress to achieve green goals, which include net-zero emissions by 2060.

We see two investible takeaways from these comments. Firstly, a continuation of the Dynamic Zero-COVID strategy would be a tailwind to our bearish 1-3-month outlook on the CNH, with a USD/CNH move towards technical resistances at 7.30 and 7.35 more likely. Secondly, the focus on core technologies is supportive of our China Hard Tech/Semiconductors sub-themes on a longer horizon.

Looking beyond the Party Congress, Asia USD bond markets fell following reports that Beijing had warned local government-backed companies against debt-financed land purchases. However, we expect the asset class impact from this to be limited given the China real estate sector's weight in the Asia USD bond benchmark is only c.3% (and the weight of High Yield bonds is only c.15%). This suggests the past week's underperformance of Asia USD bonds was likely exacerbated by poor sentiment and liquidity. Year-to-date, Asia USD bonds have outperformed global bonds, albeit with both recording negative total returns. We retain a constructive view on Asia USD bonds, given accommodative policy settings in China and our preference for Investment Grade corporate bonds.

The equity market has reacted in disappointment so far, with MSCI China testing the year's low, and rising geopolitical risk in the form of US semiconductor export restrictions did not help either. We expect Asia ex-Japan to outperform global equities over the next 12 months, given the starting point of more attractive valuations today and accommodative Chinese policies. The extremely one-sided (bearish) investor position (based on our proprietary investor diversity measure) argues that the room for a rebound exists in the short term, though a turn in the USD is likely needed to unlock Asia ex-Japan's relative outperformance in the medium term.

— Han Zhong Liang, Investment Strategist

### USD/CNY is likely to make a move towards next resistance at 7.35

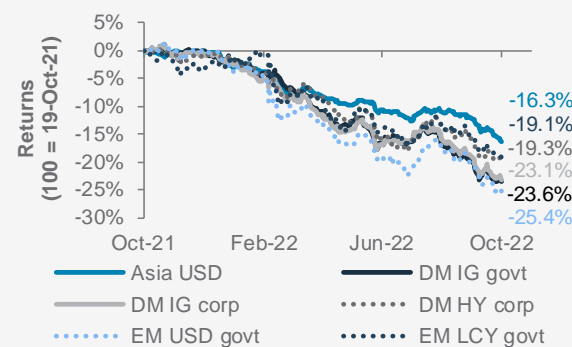
USD/CNY



Source: Bloomberg, Standard Chartered

### Asia USD bonds outperformed other fixed income sub-asset classes in the past 1 year

Normalized returns of fixed income sub-asset classes



Source: Bloomberg, Standard Chartered

### MSCI China is currently testing support at HKD 53, with the next support at 2016 low of 48

MSCI China index



Source: Bloomberg, Standard Chartered

## Top client questions (cont'd)

### Q What can we learn from the US earnings season so far?

It is early days in this quarter's US earnings season, with only 18% of companies in the S&P500 having reported so far. According to Refinitiv, 75% of companies that have reported beat earnings expectations, above the long-term average of 66%. Companies that reported have delivered a 5.7% earnings surprise. In the financial sector, where reporting is most advanced (41% of companies have reported), companies have reported an 7.6% earnings surprise. Overall, for the S&P500, Q3 is currently expected to deliver 3.1% earnings growth, notably less than the expected 9.7% revenue growth, as profit margins decline.

Despite a positive start so far, S&P500 earnings growth for the full year 2022 and 2023 continues to be revised down with an uneven sector impact. Earnings growth in 2023 for discretionary, energy, financials and utilities have been revised up, while the remaining seven sectors saw downward revisions, compared with the start of the month. Estimated 2023 growth is still reasonably robust at 7.3%, although this may come down as the earnings season progresses and companies guide lower amid expectations of an economic slowdown. We are cautious on US equities for the remainder of the year, given front-loaded rate hikes from the Fed, but we expect US equities to perform in line with global equities over the next 12 months, consistent with our core holding view.

— Fook Hien Yap, Senior Investment Strategist

### Q What is the outlook for US Treasury yields after the recent run-up?

The 10-year US Treasury yield surged past 4% this week, rising above its key resistance level of 4.14%. In our assessment, the move is largely attributable to stronger-than-expected US inflation data, with the relatively weak housing and mortgage data limiting the size of the move higher.

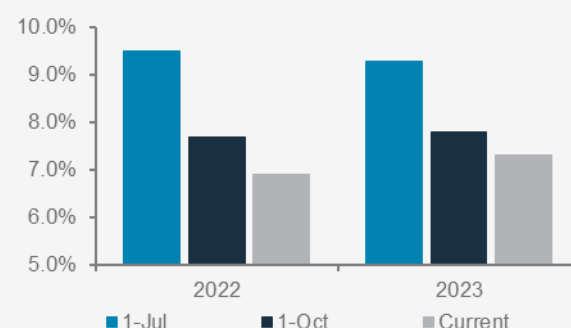
The upside inflation surprise fuelled further expectations of a more hawkish Fed, as reflected by (1) Market estimates of the Fed terminal rate by May 2023 shifting higher to 5%, approximately 40bps above the Fed's projected target rate; and (2) investor positioning data (CFTC) that has remained net-short US government bonds.

As we noted last week, limited moves in the US 10-year yield above the 4% level remain possible, with technical levels at 4.14% and 4.34%. However, we continue to see such rises in yields as opportunities to add to high quality Investment Grade corporate bonds, given the attractive yield on offer now.

— Cedric Lam, Senior Investment Strategist

**Consensus 2022 and 2023 earnings growth have been revised down since mid-2022. Current estimates still indicate growth in 2023 is likely to be similar to that in 2022**

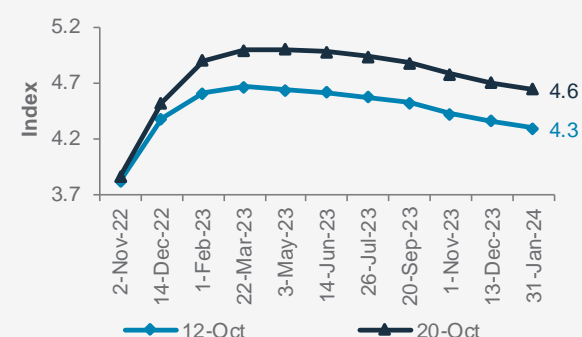
Consensus S&P500 earnings growth in 2022 and 2023 at different points of the year



Source: Refinitiv, Standard Chartered

**Market expectations of Fed rate hikes have shifted higher year over the past week**

Money market expectations of the Fed's benchmark rate until early 2024



Source: Bloomberg, Standard Chartered

## Top client questions (cont'd)

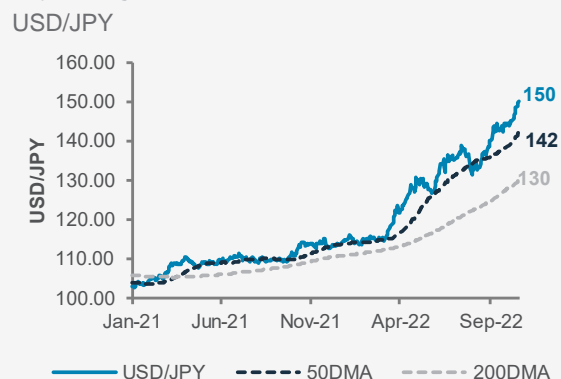
**Q Do you expect JPY and GBP to bottom soon after the recent sharp moves?**

USD/JPY rose above 150 amid the current bout of USD strength, a level last seen in 1990. Over the past week, Japan's Finance Minister Suzuki publicly commented several times that he was closely observing the FX market and he was concerned about the one-sided moves in the JPY. This, along with recent memories of intervention in September, has led to heightened speculation of another round of intervention to support the JPY. We still believe that while any such move may offer temporary relief, the stark divergence between the monetary policies of the Fed and the BoJ is likely to maintain upward pressure on USD/JPY. We see 150.40 as a near-term resistance level, followed by a stronger resistance around the 155 region.

GBP/USD edged lower this week, despite a slew of announcements by the new UK Finance Minister Jeremy Hunt, reversing most of the previously announced tax cuts, followed by the resignation of PM Truss. Truss's departure after only 45 days in office increases political uncertainty, at least until the Conservative Party elects its third PM in three months (likely in a week's time). Meanwhile, Hunt, who is likely to continue as the Chancellor in a new government, has signalled more painful spending cuts would be needed to balance the UK budget. From a fundamental perspective, we believe the GBP's recovery to close to pre-budget announcement levels underestimates the damage done to investor confidence and the underlying weak economic backdrop. Thus, while we do not rule out a retest of the 1.14 level, we remain sellers of GBP/USD on any bounce, with 1.10 and 1.07 being key technical levels.

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

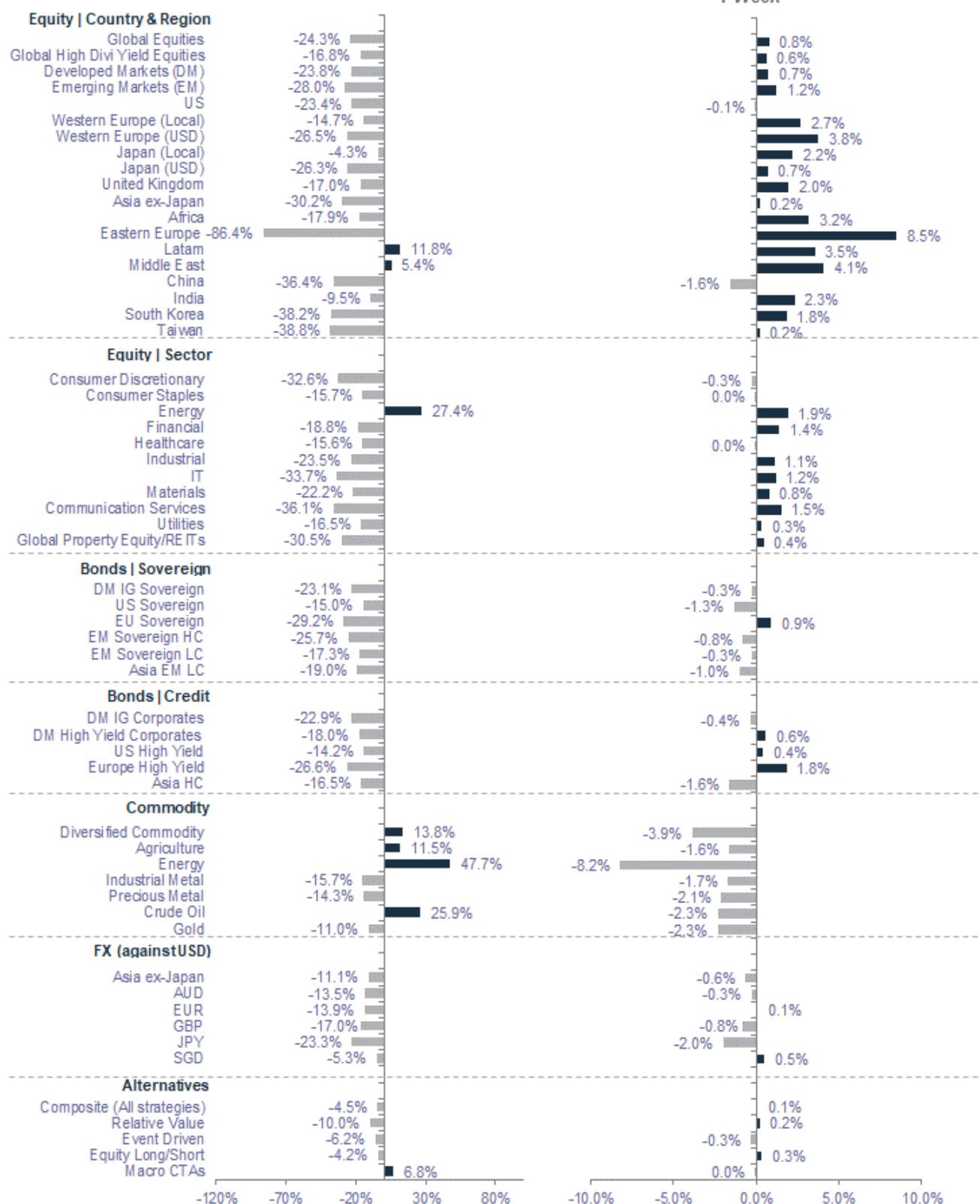
**Chances of an intervention by Japanese authorities have risen as USD/JPY tests a key psychological resistance at 150**



Source: Bloomberg, Standard Chartered

## Market performance summary \*

2022 YTD



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 20 October 2022; 1-week period: 13 October 2022 to 20 October 2022

### Our 12-month asset class views at a glance

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

Source: Standard Chartered Global Investment Committee

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

### Next resistance for the S&P500 index is at 3,729

Technical indicators for key markets as of 20 October close

Index	Spot	1st support	1st resistance
S&P 500	3,666	3,593	3,729
STOXX 50	3,493	3,406	3,536
FTSE 100	6,944	6,881	6,975
Nikkei 225	27,007	26,410	27,430
Shanghai Comp	3,035	3,006	3,075
Hang Seng	16,280	16,069	16,703
MSCI Asia ex-Japan	540	535	549
MSCI EM	865	853	878
WTI (Spot)	86	83	89
Gold	1,628	1,615	1,654
UST 10y Yield	4.23	4.04	4.32

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	EC	S&P Global Eurozone Manufacturing PMI	Oct P	–	48.4
	EC	S&P Global Eurozone Services PMI	Oct P	–	48.8
	UK	S&P Global/CIPS UK Manufacturing PMI	Oct P	–	48.4
	UK	S&P Global/CIPS UK Services PMI	Oct P	–	50.0
	US	Chicago Fed Nat Activity Index	Sep	–	0.0
	US	S&P Global US Manufacturing PMI	Oct P	–	52.0
	US	S&P Global US Services PMI	Oct P	–	49.3
TUE	US	Conf. Board Consumer Confidence	Oct	105	108
WED					
THU	EC	ECB Deposit Facility Rate	27-Oct-22	–	0.8%
FRI/SAT	US	PCE Core Deflator y/y	Sep	5.2%	4.9%
	US	PCE Deflator y/y	Sep	6.3%	6.2%
	US	Employment Cost Index	3Q	1.2%	1.3%

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 has narrowed for Asia ex-Japan equities

Our proprietary market diversity indicators as of 20 October

Level 1	Diversity	1-month trend	Fractal dimension
Global Bonds	●	↓	1.34
Global Equities	●	↓	1.47
Gold	●	↓	1.54
<b>Equity</b>			
MSCI US	●	→	1.55
MSCI Europe	●	↓	1.42
MSCI AC AXJ	●	↓	1.28
<b>Fixed Income</b>			
DM Corp Bond	●	↓	1.36
DM High Yield	●	↓	1.63
EM USD	●	↓	1.53
EM Local	●	↓	1.52
Asia USD	●	↓	1.50
<b>Currencies</b>			
EUR/USD	●	↓	1.43

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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