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Wealth Management Chief Investment Office
9 September 2022

Weekly Market View

What do jumbo hikes mean for investors?

→ Earlier this month, we further de-risked our overall market allocation after an unmistakably hawkish tone at the Fed's annual Jackson Hole symposium.

→ This week's policy moves show central banks mean business – the ECB hiked rates by a record 75bps, the BoC delivered a similar-scale hike and the RBA raised rates by 50bps. The BoE is expected to hike 50-75bps next week, followed by a 75bps hike by the Fed the week after.

→ The key question now is: will the increasingly hawkish turn in monetary policy cause a global recession? If so, will that sustain the USD's record-breaking rally that has caused global financial conditions to tighten? In this report, we attempt to answer these questions and lay out a roadmap for investors, highlighting our chosen regions and sectors.

What is your outlook for Hong Kong/China equities with the Hang Seng index testing 19,000?

What is the outlook for UK equities and GBP under new PM Truss?

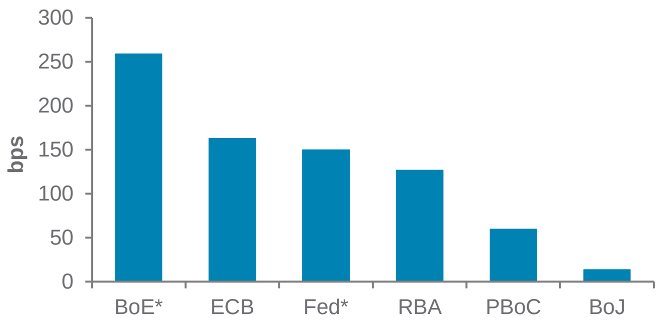
Do you expect Indian equities to continue outperforming global peers?

Important disclosures can be found in the Disclosures Appendix.

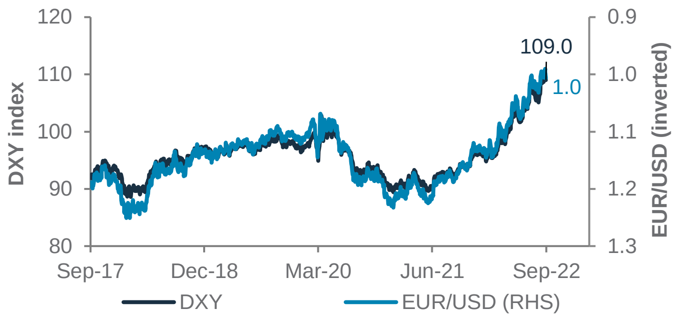
Charts of the week: Will ECB rate hikes help end the USD rally?

Markets expect the BoE and the ECB to hike rates faster than the Fed in the coming year; this could end the USD rally

Market estimates of central bank rate changes in 12 months*



USD (DXY) index and EUR/USD



Source: Bloomberg, Standard Chartered; *BoE and Fed rate hike expectations include the 65bps and 75bps hikes expected this month

Editorial

What do jumbo hikes mean for investors?

Earlier this month, we further de-risked our overall market allocation after an unmistakably hawkish tone at the Fed's annual Jackson Hole symposium. With the sole exception of the BoJ, global central bankers at the event sounded determined to take their policies to restrictive territory to tame inflation running at multi-decade highs even if it causes a sharp slowdown in growth. As a result, within a broadly balanced global asset allocation, we downgraded Euro area equities and Developed Market (DM) High Yield (HY) corporate bonds to fund an upgrade to DM Investment Grade (IG) corporate bonds.

This week's policy moves show central banks mean business – the ECB hiked rates by a record 75bps, the BoC delivered a similar-scale hike and the RBA raised rates by 50bps. The BoE is expected to hike 50-75bps next week, followed by a 75bps hike by the Fed the week after (especially if next week's core inflation data shows no marked slowdown). The key question now is: will the increasingly hawkish turn in monetary policy cause a global recession? If so, will that sustain the USD's record-breaking rally that has caused global financial conditions to tighten? The answer to these questions will likely determine whether to de-risk further or to wade back into riskier assets.

The odds of a global recession have risen significantly in recent months, especially in the Euro area where our Global Investment Committee assigns a 60% probability of a recession in the coming year (in comparison, we assign a 50% chance to a US recession). The Euro area faces a dual shock from the energy crisis because of the plunge in Russian gas supplies and the ECB's embarkation on an aggressive rate hiking cycle to tame inflation. This explains our downgrade to Euro area equities to "less preferred" from a "core holding". The increasing recession risk in the US, as the Fed tightens policy to cool the job market and wage pressures, has also led us to climb up the quality ladder in bonds – downgrading HY corporate bonds to "core holding" from "preferred" and upgrading IG corporate bonds to "core holding" from "less preferred".

The Euro area's challenges have ramifications beyond the region. The EUR's 12% slump against the USD this year to a 20-year low around parity (besides the JPY's 20% drop) is one of the primary drivers of the USD's sustained strength, given the EUR's significant weight in broad USD indices. A stronger USD, in turn, has caused global financial conditions to tighten. Although the USD is overvalued, we expect further USD strength in the next 1-3 months. The significant challenges faced by the rest of the world (Europe's energy crisis, China's COVID-19 lockdowns) have cemented the US's status as a safe haven. The Fed continues to add fuel to the rally, with the market expecting another 75bps rate hike later this month.

However, beyond the next 1-3 months, we expect the EUR and other major currencies to turn around and the USD rally to fizzle. The ECB's 75bps rate hike this week is a decisive step as the central bank turns its focus singularly on lowering inflation, even at the cost of growth. Money markets are now pricing a more aggressive ECB rate hiking cycle (163bps in 12 months) compared with other major central banks, including the Fed (see chart above). This would narrow rate differentials with the US. Moreover, European governments are increasingly willing to fiscally support industries and consumers to shield them from the energy crisis – Germany's EUR 65bn energy package this week is the first step. The US, in contrast, faces a government gridlock after the November mid-term elections where Democrats are expected to lose majority in Congress.

Meanwhile, we expect China's tight COVID-19 lockdowns – which have been followed by strict travel advisory during the upcoming holidays - to ease once the Party Congress is over in October, even as the government and the central bank stimulate domestic consumption and infrastructure spending. A policy-driven gradual recovery in China is likely to encourage capital flows to rotate away from the US. We believe Asia ex-Japan stands out as the likely beneficiary of such flows due to historically cheap valuations. This explains our preference for the region's equities and bonds (see pages 4-6 for details).

— 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.

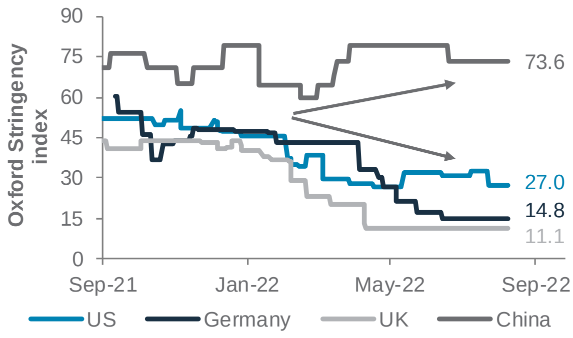
(+) factors: Strong US labour, services PMI; supportive China policies

(-) factors: China lockdown; Russia gas flow halt; ECB, RBA, BoC hikes

	Positive for risk assets	Negative for risk assets
COVID-19	• China new cases are slowing down • Hong Kong Chief Executive John Lee acknowledged plans to ease COVID-19 curbs	• China extended lockdowns in key cities; tightened restrictions during the upcoming holiday season • Hong Kong new cases surged
	Our assessment: Negative – Extended China lockdowns	
Macro data	• US new job creation stronger than consensus, with the unemployment rate rising due to a higher labour force participation rate • US ISM services rose unexpectedly • China Caixin services PMI higher than forecast • Fed's Beige Book revealed moderating inflation • China inflation slowed unexpectedly	• China exports slowed more than expected • Euro area PPI rose more than expected • Euro area Sentix Investor Confidence fell more than consensus • Euro area retail sales growth accelerated, but less than expected
	Our assessment: Neutral – Strong US labour data, services PMI; strong China services PMI versus slowing China exports, falling Euro investor confidence, retail sales	
Policy developments	• China's policymakers committed to accelerate policy support in Q3 22 • China cut FX reserve requirements to prop CNY • New UK PM Liz Truss to cap energy costs	• ECB hiked rates by 75bps • RBA hiked rates by 50bps • BoC hiked rates by 75bps
	Our assessment: Neutral – Supportive China policies, UK cap on energy costs versus ECB, RBA and BOC rate hikes	
Other developments	• Euro area energy ministers are meeting on Friday to discuss emergency interventions	• Russia halted Nord Stream 1 gas flow indefinitely allegedly due to a lack of turbines
	Our assessment: Negative – Indefinite cut to Nord Stream 1 flow	

China's tight mobility restrictions have contrasted sharply with easing restrictions elsewhere

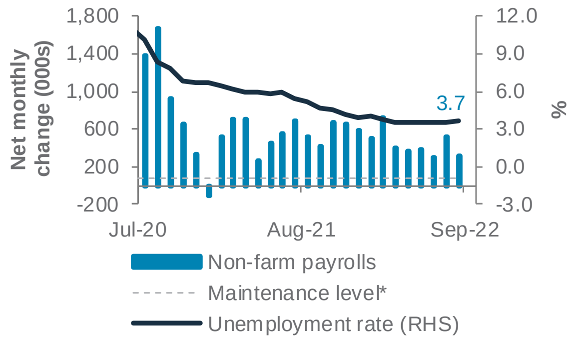
Oxford Stringency index



Source: Bloomberg; Standard Chartered

US job creation needs to slow significantly in the coming months to cool wage pressures and enable the Fed to slow the pace of rate hikes

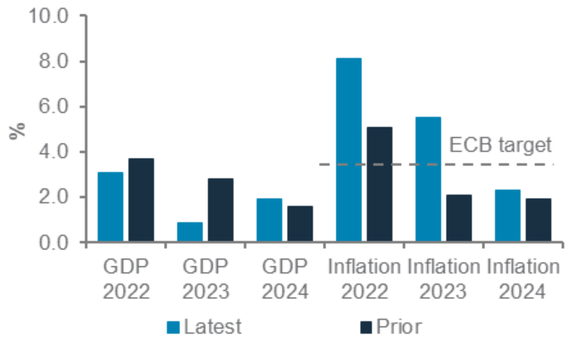
US net new monthly jobs, unemployment rate



Source: Bloomberg, Standard Chartered
* Job creation required to maintain the current level of unemployment rate, based on Atlanta Fed's jobs calculator

The ECB cut Euro area growth and raised inflation estimates as it hiked rates by 75bps this week

ECB's new growth, inflation and policy rate projections



Source: Bloomberg, Standard Chartered

Top client questions

What is your view on China equities with the Hang Seng index testing 19,000 level this week?

The Hang Seng index, which represents China's offshore equities, has been suffering over the last few weeks: (1) ADR delisting – there has been progress regarding the inspection of the audit work of US-listed Chinese companies. However, the US SEC warned earlier this week US accounting firms that agree to lead audits of Chinese ADRs may be breaching US rules if they fail to fully seek a range of information, such as the integrity of the issuer's management; (2) policy stimulus – the move to cut foreign currency reserve requirements earlier this week did not stop CNY weakness versus the USD; and (3) policy restrictions – an announcement discouraging domestic travel and gatherings until the end of October to control COVID-19 ahead of the Party Congress risks delaying the economic recovery.

Looking beyond these short-term issues, we believe authorities are likely to concentrate on revitalising the economy after the Party Congress. Divergent economic policies – policy support in China versus policy tightening in the US – remains a major tailwind for China risk assets. China's equity valuations continue to be attractive compared to global equities. We also prefer onshore equities, which are less susceptible to geopolitical tensions, versus offshore peers.

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

China's equities are trading at a nearly 26% 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

What is your view on the CNY with the PBoC's latest policy adjustment?

The CNY has depreciated by almost 10% against the USD this year due to two main factors: (1) USD strength, which has been a headwind to currencies across the board; and (2) narrowing yield differentials between US and China bonds as Chinese authorities ease monetary policy to support growth, while the Fed tightens.

The PBoC announced a 2% cut to FX reserve requirements for banks starting 15 September; this is likely to alleviate onshore USD liquidity to a certain degree. In addition, the central bank has been fixing the daily reference rate at a much stronger level than the average forecast for the past 12 consecutive days.

In our assessment, while these measures can help slow CNY weakness, it is difficult for the currency to reverse direction in the short term in the face of continued USD strength. The cut in the FX reserve requirement would release about USD 19bn (based on end-July data), which remains small relative to cross border receipts. The stronger fixing bias has had a limited impact thus far.

From a technical standpoint, initial resistance is around the psychological 7.00 level. A break of that level could see USD/CNH test the next resistance at 7.1965. On the downside, we see strong support around the previous peak of 6.8370.

— **Zhong Liang Han,** *Investment Strategist*

Key resistance for USD/CNH is at 7.00; a break higher could lead to a likely test of 7.1965

USD/CNH

Source: Bloomberg Standard Chartered

Top client questions (cont'd)

What is the outlook for UK equities and the GBP under the new Prime Minister Liz Truss?

PM Truss's proposed energy cap is likely to increase UK consumers' disposable income and lift consumer-based domestic equity sectors. While this is a positive, larger UK companies are more dependent on non-UK earnings, with 70% of the earnings of the FTSE-100 index coming from overseas. Thus, weakness in the GBP versus global currencies is arguably an important positive driver of UK equities. We see more weakness in the GBP as long as it remains below 1.1970 due to UK's high inflation and weak economic outlook.

UK equities remain a preferred market. PM Truss's appointment puts political uncertainty behind us. Other key positives include: (1) the dominance of the three "old economy" sectors – financials, energy and materials – which comprise around 40% of the index. These sectors may outperform as inflation returns and yields are no longer at ultra-low levels; (2) cheap valuations – on an absolute basis, the 12-month forward P/E for the MSCI UK is at 9.1x, which is around a 20-year low. The UK's relative valuation versus global equities has fallen to a 36% discount from an 7.4% premium in 2016 – this is its deepest discount in 20 years; and (3) UK equities offer a 12-month dividend yield of 4.5%, well above the MSCI All-country world index's dividend yield of 2.4%.

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

What is your view on the JPY, and what are some factors that could alter the BoJ's easy monetary stance?

We believe USD/JPY could remain elevated over a shorter 1-3 month horizon, underpinned by a stronger USD and widening interest rate differentials. Markets are anticipating a more hawkish Fed, whereas the BoJ has stubbornly held to its easy monetary policy.

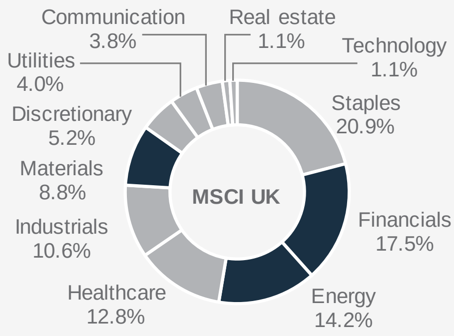
A change in the BoJ's stance would likely be needed as a catalyst for a sharp move lower in USD/JPY. While there are long-term questions about the sustainability of the BoJ's policies or the gap between the Fed's policy stance and the BoJ's, a sharp U-turn in Japan looks unlikely for now, with Japan's inflation expectations still below the 2% inflation target. Although rising energy costs have been a key contributor to higher headline inflation, measures to reduce Japan's reliance on crude oil – by increasing LNG exports from the US and ramping up nuclear power production – mean inflation expectations have not been lifted significantly higher.

However, some short-term respite in the USD/JPY uptrend is possible given that JPY weakness over the past week has raised concerns from the Japanese cabinet, increasing the risk of an intervention. Technical levels to watch include support around the previous high of 139.35 and key resistance at the previous peak of 147.75.

— **Nataniel Tang,** *Investment Strategist*

UK equities are heavily weighted towards "old economy" sectors…

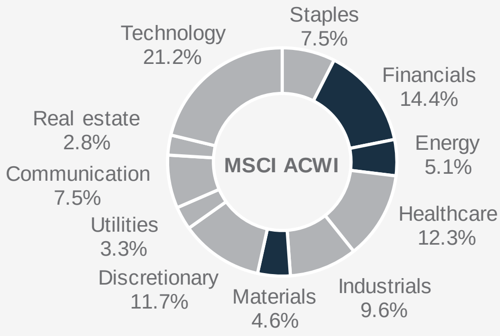
Sector composition in MSCI UK



Source: Bloomberg, Standard Chartered

… while global equities have higher weightings in "new economy" sectors

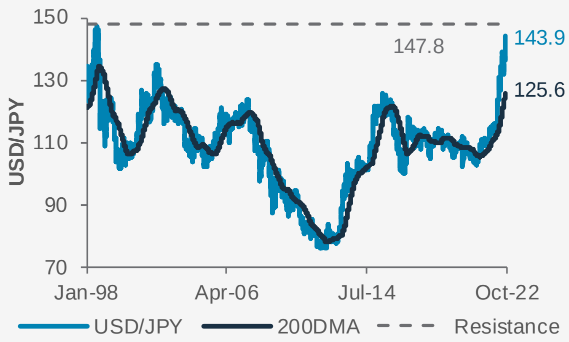
Sector composition in MSCI All-country World



Source: Bloomberg, Standard Chartered

Key resistance for USD/JPY is at 147.75, a level last seen in 1998

USD/JPY with technicals



Source: Bloomberg, Standard Chartered

Top client questions (cont'd)

Do you expect Indian equities to continue outperforming global peers? What are your sectoral preferences?

Indian equities have continued to outperform peers this year, up 2.7% YTD in USD terms versus drops of over 20% for its Asia and Emerging Market (EM) peers (based on the performance of the MSCI India, the MSCI Asia ex-Japan and the MSCI Emerging Markets indices). India remains a preferred market in Asia, and we remain constructive on Indian equities due to the following factors:

1) **A robust economic growth outlook.** High frequency economic indicators, such as PMI, industrial production, vehicle sales, power demand, continue to signal above-trend domestic economic growth. We expect GDP growth to remain above 7% for the fiscal year ending March 2023, supported by greater public investments, resilient consumption and nascent signs of a revival in private capex.

2) **Superior earnings delivery.** India's earnings growth continues to outperform relative to peers, with expectations of a third consecutive year of double-digit EPS growth (17% for the fiscal year ending March 2023) for the benchmark Nifty index. Further, the pace of earnings revisions continues to stay positive.

3) **Repricing of higher rates appear reasonably factored in.** In our view, markets have priced in a significant part of likely central bank rate hikes, with the one-year Overnight Indexed Swap (OIS) spread suggesting market participants expect the RBI to raise policy rates by at least 75bps over the next 12 months.

4) **Domestic equity market flows.** Stable domestic equity inflows and a structural shift in household savings towards financial assets continue to be key supports for the market. The recent resumption of foreign inflows into Indian equity markets (start of a reversal following earlier outflows of about USD 35bn over October 2021 to June 2022) is an additional tailwind.

However, key risks, including a slowing global economy, hawkish central banks and India's higher valuation premium to peers, are likely to keep volatility elevated. We prefer large cap equities and maintain a domestic cyclical sector (financials, consumer discretionary and industrials) bias given the above macro environment. Further, relative earnings and valuations remain favourable for these sectors.

Finally, on the INR, downside risks emanating from deteriorating external accounts given rising import demand, still-elevated crude oil prices and lower INR carry spreads are offset by above-trend growth, improving real yields and light foreign investor positioning in equity and bonds. In the near term, a resumption of foreign investor inflows, a correction in crude oil prices and superior growth compared to peers are likely to support the INR.

— **Vinay Joseph,**
Head, Investment Products and Strategy, India

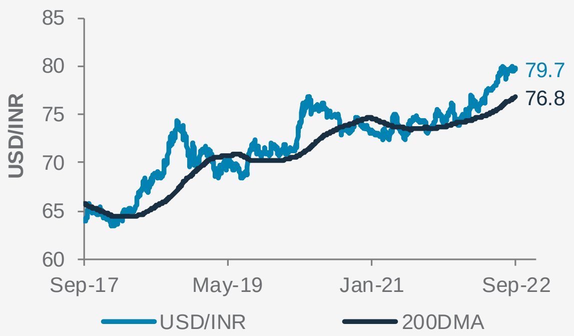
Indian equities have outperformed global and Emerging Market peers over the past year

One-year relative performance of MSCI India, China, Asia ex-Japan and All Country World indices

Source: MSCI, Bloomberg, Standard Chartered

The INR has depreciated this year due to India's deteriorating external balances as a result of higher oil prices and narrowing rate differentials

USD/INR



Source: Bloomberg, Standard Chartered

Top client questions (cont'd)

What is the outlook for oil?

Crude oil (WTI) prices have trended lower on fears of slowing demand as a hawkish Fed raises the risk of an economic recession. Markets are currently more concerned about demand softness versus supply side constraints, with WTI oil prices paring strong gains on Monday despite OPEC+ announcing a 100k bpd output cut in October. Stringent lockdowns in China have exacerbated demand concerns, especially with China's crude oil imports falling 9.4% y/y in August.

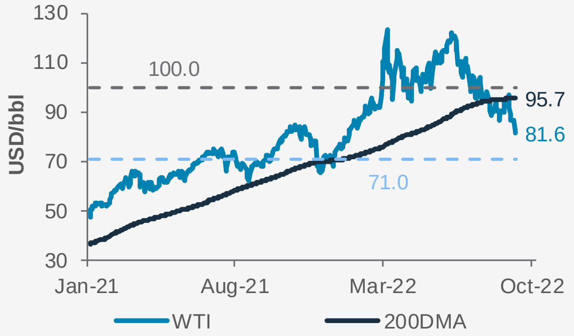
However, we remain constructive on oil over a three-month horizon. We believe recession-linked demand fears are likely overdone. Demand for oil remains moderately supportive, with crude oil stocks in the US Strategic Petroleum Reserve down roughly 25% YTD. On the supply side, the chances of a deal being reached with Iran appear to be fading, and a proposed Russian oil price cap could further restrict supply, both posing upside risks to oil.

On technicals, 82 remains a key level for oil, and a sustained break below could see it test 71. A break above 100 could mean that the near-term downtrend has faded.

— **Nataniel Tang,** *Investment Strategist*

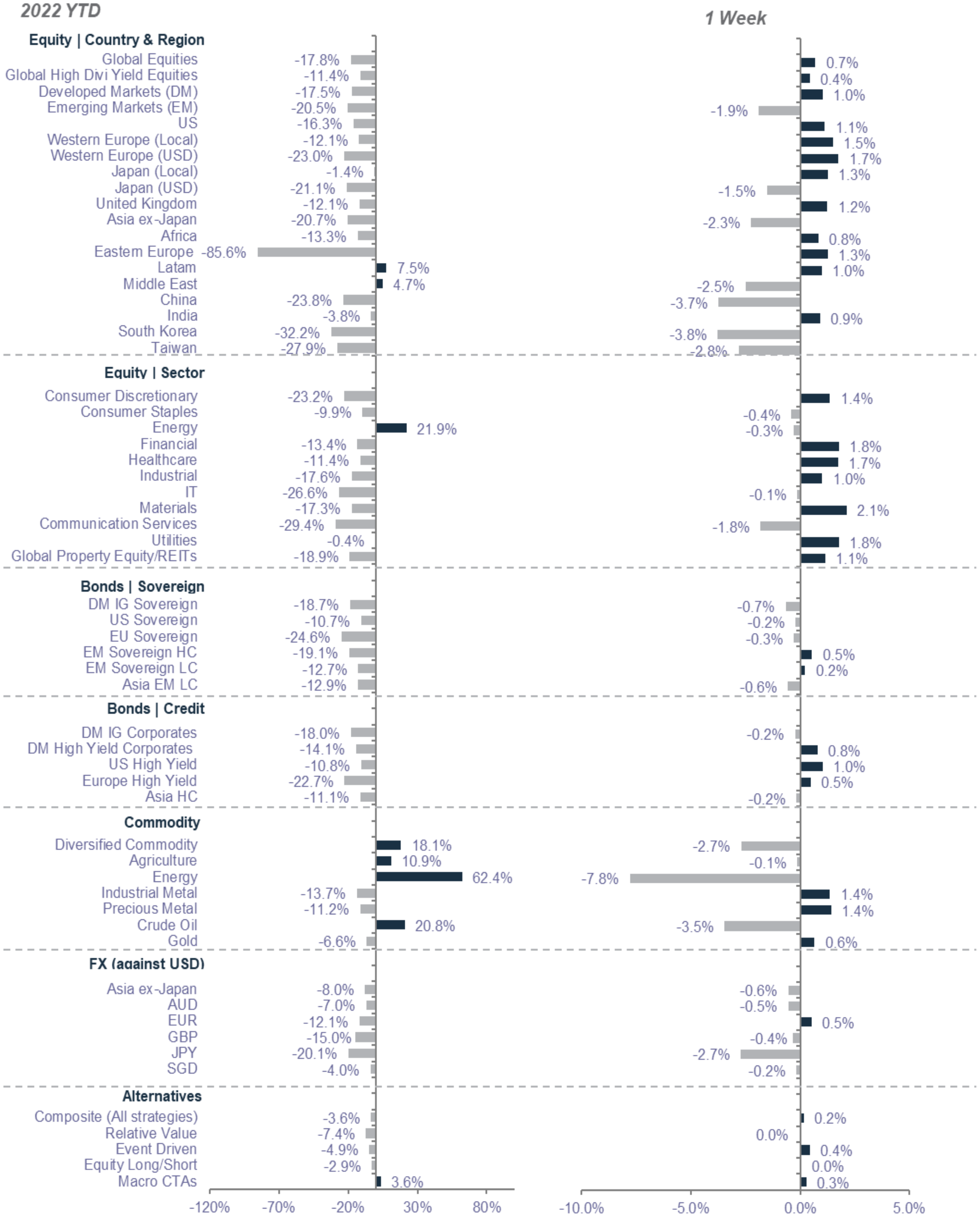
We remain constructive on crude oil as long as support of 71 holds; a break above 100 could indicate that the near-term downtrend has faded

Oil (WTI) with technicals



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 08 September 2022; 1-week period: 01 September 2022 to 08 September 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	UK	ILO Unemployment Rate 3Mths	Jul	–	3.8%
	EC	ZEW Survey Expectations	Sep	–	-54.9
	US	CPI y/y	Aug	8.1%	8.5%
	US	CPI Ex Food & Energy y/y	Aug	6.1%	5.9%
WED	UK	CPI y/y	Aug	–	10.1%
	UK	CPI Core y/y	Aug	–	6.2%
	US	PPI Ex Food & Energy y/y	Aug	–	7.6%
	US	PPI Final Demand y/y	Aug	–	9.8%
THUR	UK	Bank of England Bank Rate	Sep	–	1.8%
	US	Empire Manufacturing	Sep	–	-31.3
	US	Retail Sales Ex Auto & Gas	Aug	0.9%	0.7%
FRI/SAT	CH	Industrial Production y/y	Aug	3.9%	3.8%
	CH	Retail Sales y/y	Aug	3.3%	2.7%
	CH	Fixed Assets Ex Rural YTD y/y	Aug	5.5%	5.7%
	UK	Retail Sales Ex Auto Fuel y/y	Aug	–	-3.0%
	US	U. of Mich. Sentiment	Sep P	59.6	58.2

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 3.38%

Technical indicators for key markets as on 8 September

Index	Spot	1st support	1st resistance
S&P 500	4,006	3,941	4,039
STOXX 50	3,512	3,487	3,541
FTSE 100	7,262	7,233	7,296
Nikkei 225	28,065	27,642	28,277
Shanghai Comp	3,236	3,199	3,259
Hang Seng	18,855	18,655	19,253
MSCI Asia ex-Japan	614	611	621
MSCI EM	957	952	967
Brent (ICE)	89.2	86.2	93.9
Gold	1,710	1,702	1,718
UST 10y Yield	3.32	3.22	3.38

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 8 September

Level 1	Diversity	1-month trend	Fractal dimension
Global Bonds	◐	→	1.38
Global Equities	●	→	1.51
Gold	◐	→	1.38
Equity			
MSCI US	●	→	1.70
MSCI Europe	◐	↓	1.36
MSCI AC AXJ	◐	↓	1.35
Fixed Income			
DM Corp Bond	◐	↓	1.43
DM High Yield	●	→	1.57
EM USD	●	↑	1.60
EM Local	◐	→	1.46
Asia USD	●	→	1.58
Commodities			
WTI Crude Oil	◐	↓	1.34

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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