



# Global Market Outlook

## Fade the “melt-up”

We continue to expect a US recession in the next 6-12 months. We favour bonds over equities, government bonds over High Yield bonds, Asian equities over US/European equities and multi-asset income strategies.

Short-term indicators warn of a temporary period of equity outperformance, the so-called “melt-up” trade. Investor positioning, in particular, is too bearish and may have to normalise first.

Such a move is likely to open an opportunity for long-term investors to rotate into our preferred assets. We expect the USD to extend its recent weakness.



Is weak market sentiment/positioning a contrarian signal?

What are the key macro factors to watch in the near term?

What are your quant models telling us?

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# Investment strategy and key themes

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## Our top preferences (12-month outlook)

### Foundation overweights

- Government bonds, gold
- *In equities:* Asia ex-Japan
- *In bonds:* Developed Market Investment Grade government, Asia USD bonds

### Sector overweights

- *US:* Healthcare, Staples, Utilities
- *Europe:* Utilities
- *China:* Comm. Services, Consumer Discretionary, Technology, Industrials

### FX views

- Modestly weaker USD

### Structural macro trends\*

- A digital tomorrow
- Preparing for an ageing world
- From unipolarity to multipolarity
- Investing in a climate-constrained world

\*Individual reports available

## Fade the “melt-up”

- We continue to expect a US recession in the next 6-12 months. We favour bonds over equities, government bonds over High Yield (HY) bonds, Asian equities over US/European equities and multi-asset income strategies.
- Short-term indicators warn of a temporary period of equity outperformance, the so-called “melt-up” trade. Investor positioning, in particular, is too bearish and may have to normalise first.
- Such a move is likely to open an opportunity for long-term investors to rotate into our preferred assets. We expect the USD to extend its recent weakness.

## Bridging the gulf between macro and market signals

**Traditional recession indicators continue to point to a relatively high probability of a US recession over the next 6-12 months.** This is illustrated by warning signs across most of our US recession checklist, a high recession probability on our quantitative model and a still-bearish signal from our growth-inflation model. Learnings from the last four US recessions inform us that an ‘un-inversion’ of the US government bond yield curve (whereby short-term yields once again fall below long-term yields) in the coming months would also signal that a recession is more imminent.

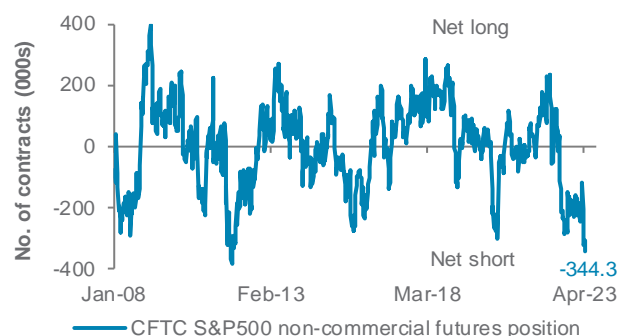
**Despite this backdrop, global equity markets have remained remarkably resilient. A robust US job market, leading to sustained consumption, and an extremely bearish investor positioning are likely behind the resilience.** Several market-based indicators are in sharp contrast with the fundamental backdrop. The S&P500 index positioning data supports anecdotal evidence that many investors have already positioned for a bearish outcome. Fund manager surveys illustrate similarly bearish sentiment. This likely points to sustained resilience, and even continuation of the ongoing rally in risk assets in the near term, because extremely bearish positioning data has historically often resulted in a short-term “melt-up” in equities.

**Technical indicators are lacklustre.** The S&P500 index is struggling to break above resistance close to 4,200, market breadth remains narrow and the technical indicator from our quantitative models remains neutral. Other short-term indicators, such as our market diversity indicator or the “Greed & Fear” index, remain largely neutral.



**Fig. 1 Net-short positions on US equities most extreme since 2011, posing risk of an extended rebound**

US CFTC investor positioning on S&P500 index futures



Source: Bloomberg, Standard Chartered

## Equities – the short-term “melt-up” trade

The figure below sums up what we see as a **gulf between long-term (6-12m) fundamental indicators and short-term (1-3m) market indicators**.

**Fig. 3 Long-term (6-12m) indicators point to a US recession and downside for risk assets, but some short-term (1-3m) market indicators remain positive**

Risk asset signals from key US macro and market indicators

6-12m fundamental indicators	1-3m technical/positioning indicators
Our recession* checklist	Equity market positioning** ▲
Our quantitative recession model	Our investor diversity model ◆
Our growth-inflation model	S&P500 technicals ◆
	Our 'Greed & Fear' index ◆
	Our equity-bond risk model (macro-based) ▼
	Our stock vs bond model (macro and market-based) ▲
	"Sell-in-May" precedence ▼

Source: Bloomberg, Standard Chartered

\*See GMO presentation for the full list of indicators on our US recession checklist

\*\* Based on positioning data, fund manager surveys

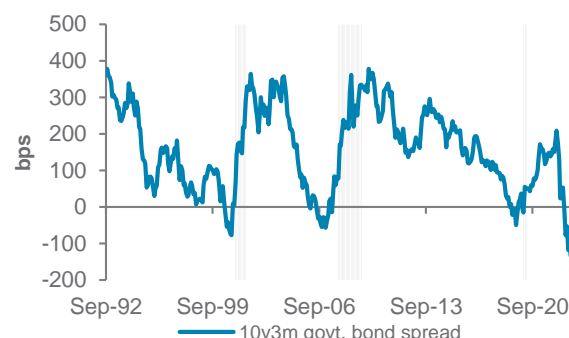
**Signal for risky assets:** ▲ Positive | ▼ Negative | ◆ Neutral

In our view, in the short term (1-3m), it is likely equities temporarily extend their recent outperformance vs bonds. A key driver of this view is the extremely bearish investor positioning. This ideally needs to normalise before equities can underperform bonds more convincingly.

Beyond this temporary move, though, we continue to favour bonds over equities as markets converge to fundamentals. While one can debate when precisely a US economic recession starts, we remain reluctant to position against fundamental indicators. We continue to be of the view that a US recession is likely over the next 6-12 months. This, in turn, is likely to result in bonds outperforming stocks as earnings expectations and bond yields move lower.

**Fig. 2 US 10y-3m yield curve continues to send a recession warning**

Spread between US 10y and 3m bond yields



Source: Bloomberg, Standard Chartered; grey bars: US recession

## Asia ex-Japan equities likely offer a rotation opportunity.

The region's equity markets have underperformed global equities as markets assign a higher geopolitical risk premium for China, despite an improving economic outlook and stronger earnings growth. We expect this risk premium to decline, especially if the USD continues to weaken. Thus, Asia's recent underperformance offers an opportunity for investors to rotate from Developed Market equities.

## Positioning less of a challenge for income

**Short-term positioning risks for high-quality bonds are more mixed.** Fund manager surveys suggest the consensus is currently positioned to favour bonds over equities, and Investment Grade (IG) bonds over High Yield bonds. However, positioning data shows investors are very net-short US government bonds. This is usually a contrarian signal for higher bond prices (lower bond yields). The 10-year US government bond yield is also struggling to break above technical resistance.

**We favour adding exposure to high-quality bonds on any rebound in yields.** While positioning data argues short-lived rebounds in bond yields are possible, especially if equity markets rebound over a 1-3m horizon, earning the yield requires staying invested for 6-12 months. This means we favour using any yield rebounds to add exposure to high-quality bonds, and income strategies more broadly, rather than trying to trade any short-term yield rebound.

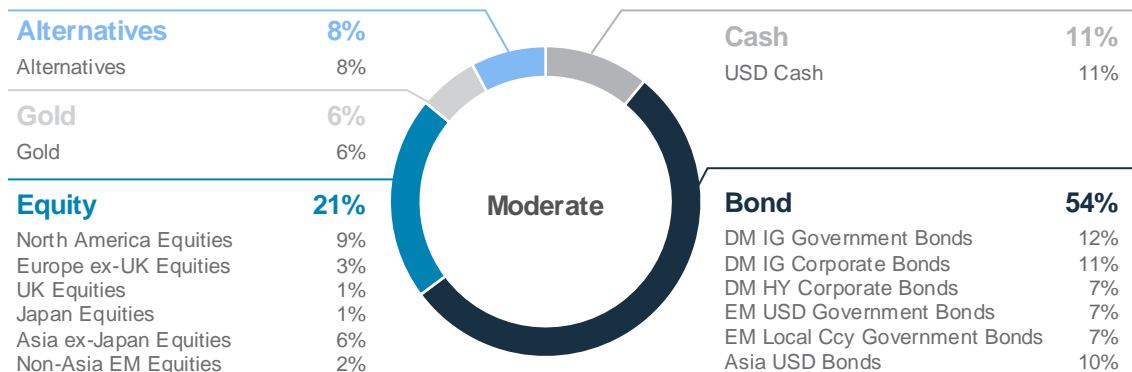
**We continue to favour Developed Market Investment Grade bonds and Asia USD bonds and stay Underweight High Yield bonds.** High Yield bonds' correlation with equities means they may be well-supported in the short term should equities temporarily rise. However, we remain Underweight this asset class and would use any rebounds to reduce exposure.

## USD weakness to extend

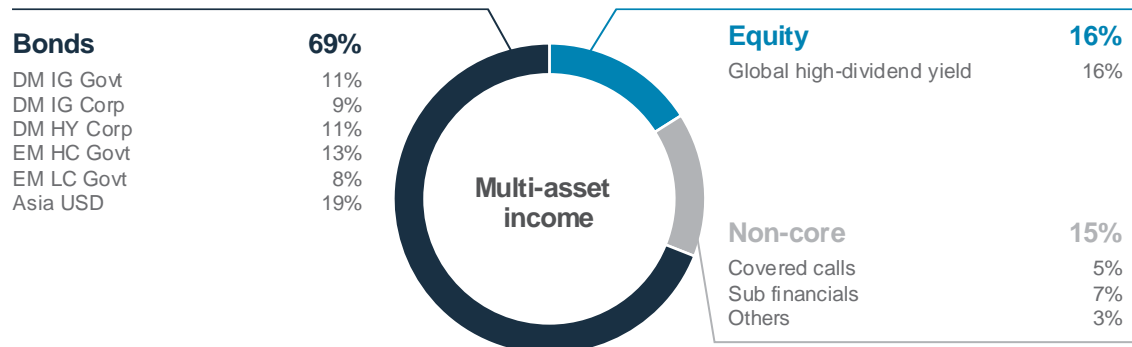
**We expect the USD downtrend to extend** as market conviction in an earlier pause in rate hikes by the Fed relative to other major central banks strengthens. This should not only lead to a rise in other G10 currencies, but also support Emerging Market assets, particularly in Asia ex-Japan.

# Foundation: Our tactical asset allocation

## Global\* allocation for a moderate risk profile



## Multi-asset income allocation for a moderate risk profile



	View	Detail
<b>USD cash</b>	◆	+ Safety, positive real yields    - Reinvestment risk, risk of long-term underperformance
<b>Bonds</b>	▲	
DM Govt	▲	+ High credit quality, outperformance during a recession    - Still-elevated inflation
DM IG Corporate	◆	+ High credit quality, moderate yields    - Fairly valued
DM HY Corporate	▼	+ Attractive yield, low rate sensitivity    - Deteriorating credit quality, wider spreads
EM USD Govt	◆	+ Attractive yield and value    - Weakening EM credit quality
EM Local Ccy Govt	◆	+ Moderate yield, potential for FX appreciation    - Higher volatility
Asia USD	▲	+ Mainly IG credit quality, declining default rates    - Fairly valued
<b>Equities</b>	▼	
North America	◆	+ Potential for Fed pivot    - US recession risk, banking sector woes
Europe ex-UK	◆	+ Resilient margins    - Still-elevated inflation, hawkish ECB
UK	▼	+ Attractive valuations, dividend yield    - Prolonged BoE tightening
Japan	◆	+ China recovery, resilient domestic demand    - Potential BoJ tightening
Asia ex-Japan	▲	+ China's reopening and policy support    - Escalating China-US tensions
<b>Gold</b>	▲	+ Falling yields, portfolio hedge    - Risk of a USD rebound
<b>Alternatives</b>	◆	+ Diversifier characteristics    - Equity, corporate bond volatility

Source: Standard Chartered Global Investment Committee; Green = Upgrade; Red = Downgrade; \*See page 15 for Asia-focused allocations

Legend: ▲ Overweight | ▼ Underweight | ◆ Neutral

# Perspectives on key client questions

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Investment Strategist

## Q Is weak market sentiment/positioning a contrarian signal?

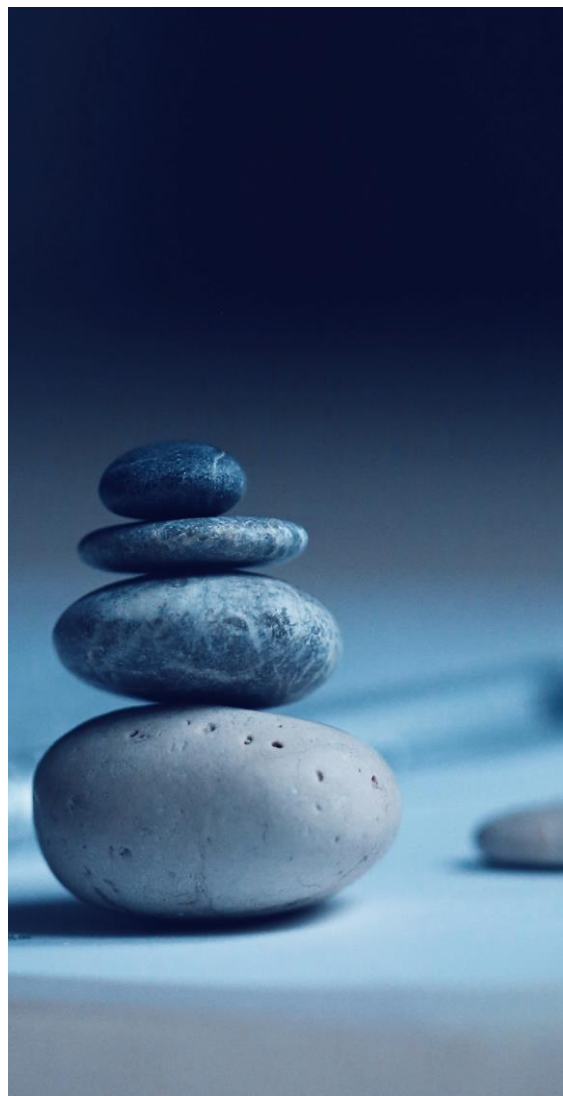
If the US economy falls into a recession, as we and the consensus expect, it would be one of the most well-forecast recessions in history. Despite gloomy expectations, risky assets have been relatively resilient, with every major asset class, besides commodities and the US dollar, advancing year-to-date and handily beating cash.

The bearish sentiment and positioning offer a possible explanation as to why risk assets have been resilient. In our Investment Strategy section, we highlighted the divergence in signals from long-term fundamental indicators and short-term technical indicators (see Figure 3). Excessively bearish investor positioning, likely due to the strong consensus of a US recession, stands out as a possibly bullish short-term signal. The bearish positioning has raised the room for disappointment, increasing the risk of a short-term re-pricing if things don't play out as expected.

### When short-term positioning collides with long-term fundamentals

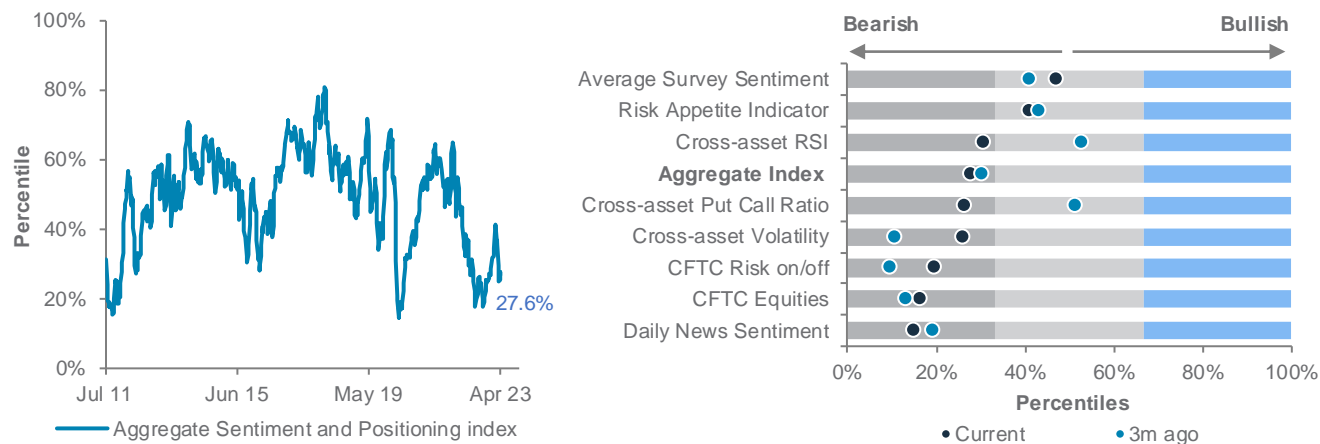
As investors, it is important to keep in mind the potential discrepancies between short-term market indicators, such as sentiment and positioning, and longer-term fundamental factors, such as growth and earnings. Often, investor sentiment can overwhelm market fundamentals in the short run, leading famed investor Benjamin Graham to declare that “in the short run, the market is a voting machine, but in the long run, it is a weighing machine.”

In this piece, we look at how various sentiment and positioning indicators stack up and what they might inform us about the short-term market outlook. We aggregated eight indicators into a single index (Aggregate Sentiment and Positioning index) and found the prevailing market sentiment to be near extreme levels of bearishness. Historically, extremes in sentiment and/or positioning have often resulted in a short-term reversal in risk assets. A possible explanation for this could be that at these levels, the number of prospective sellers or buyers respectively diminishes, leaving the market vulnerable to a counterintuitive move in the opposite direction.



**Fig. 4 An aggregated index of eight positioning and sentiment indicators points towards pessimism in the markets**

Aggregate Sentiment and Positioning index and the current and three-month prior readings of eight component indicators



Source: Bloomberg, Standard Chartered.

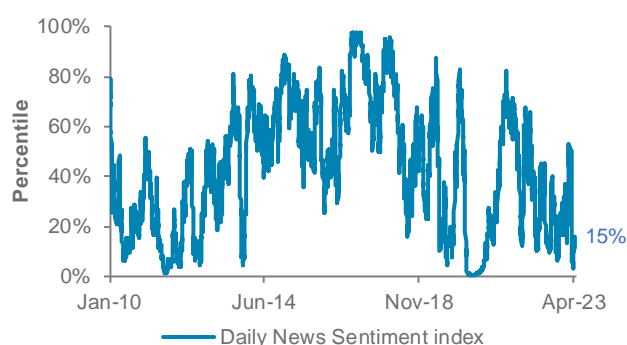
## Survey and news sentiment remains downbeat

Measuring market sentiment can be a challenging undertaking. Nevertheless, there are indicators that can provide insights into the prevailing mood of the market. These indicators can be broadly categorised into sentiment- and positioning-based indicators, as well as cross-asset hybrids that incorporate the elements of both.

Our Average Survey Sentiment indicator aggregates the results of two closely watched surveys, the AAI Investor Sentiment Survey and NAAIM Exposure Index, to gauge the sentiment of both individual investors and active managers, respectively. The surveys are not meant to be predictive; but rather to help investors manage risk and stay informed. Separately, the Daily News Sentiment Index, developed by the Federal Reserve Bank of San Francisco, analyses economics-related news articles to capture the economic mood in the US.

**Fig. 5 Economic sentiment in the media remains depressed near COVID-19 lows and has weighed on investor sentiment**

Daily News Sentiment Index



Source: Federal Reserve Bank of SF, Standard Chartered

## Investors are positioned for a bearish outcome

Unlike sentiment surveys that describe the market's view, positioning data reveals it through actual trading positions. Statistics provided by the Commodity Futures Trading Commission (CFTC) and various options exchanges offer

insights into how investors are currently positioned in various markets, with the number of opened longs or shorts in an asset indicating the bullish or bearish views of investors. Our Put-Call ratio (PCR) and CFTC risk on/off indicators leverage these data to provide insights into current market positioning.

Both indicators currently point towards investors' bearishness in risk assets as scepticism has grown over the durability of 2023's equity advance. Speculators have increased their net short positions in the S&P500 to multi-year highs. However, the prevailing caution may set the stage for a market bounce, as at extreme levels of positioning, the number of prospective sellers diminishes, making the market vulnerable to a rebound. This was the case in recent months when the CFTC risk on/off indicator reached extreme lows just as recession fears receded, sparking a rally in the S&P500 index.

## Extreme pessimism may signal upside risks short term

Our analysis shows that there is predictive power for subsequent returns when sentiment is at extreme levels. When the Aggregate Index (Fig 4) troughs below the 20th percentile, it usually indicates that markets have already experienced a large correction and that the asymmetry of returns is positive. On average, the MSCI ACWI gained 16% in the subsequent six months. The opposite also holds true, with MSCI ACWI retreating, on average 6.7%, three months after the Aggregate Index peaked above its 70th percentile.

## Being contrarian is not a guaranteed success

Positioning and sentiment data can be used to identify potential areas of crowded trades or extreme sentiment. For example, if net-short position in the S&P500 index is near an extreme and sentiment bearish, but prices are advancing, this will increase the risk of investors liquidating their short positions, thus sustaining the rally in the near term.

However, being contrarian alone is not a fool proof recipe for success. At times, the hype or fear in the market can be well-justified. Hence, we favour placing the signal from positioning data within a more holistic approach (Figure 3).

**Fig. 6 Extreme levels of the Aggregate Sentiment and Positioning index can provide contrarian signals**

Subsequent month average returns of the MSCI ACWI at different peak and trough percentiles of the Aggregate Index

Aggregate indicator	MSCI ACWI returns in the next:			Hit ratio of positive returns in the next:		
	1 month	3 months	6 months	1 month	3 months	6 months
<b>Troughs</b>						
Between 20-30th percentile	6.59%	9.42%	12.37%	100%	100%	100%
Below 20th percentile	8.45%	9.80%	15.92%	100%	80%	100%
<b>Peaks</b>						
Between 60-70th percentile	-1.77%	-1.88%	-1.28%	25%	25%	50%
Above 70th percentile	-2.90%	-6.74%	0.73%	0%	25%	50%

Source: Bloomberg, Standard Chartered

# Macro overview – at a glance

Rajat Bhattacharya  
Senior Investment Strategist



## Key themes

**China to outperform as global growth slows:** Global growth is set to slow this year as the initial spurt in consumption following the taming of the COVID-19 pandemic dissipates across Developed Markets (DM). The IMF cut global growth estimates for this year to 2.8%, from last year's 3.4%. Developed economies are projected to grow 1.3% this year vs last year's 2.7%. However, we expect China's economy to outperform as activity normalises. In fact, China's stronger-than-expected 4.5% y/y growth in Q1 adds upside risks to our full-year growth forecast of 5%. The US hitting its debt ceiling is a key near-term downside risk.

**Inflation to trend lower but remain above target:** Inflation continues to soften globally as supply bottlenecks for goods normalise. However, tight job markets in the US and Europe mean service sector-led inflation is likely to remain elevated and well above the central banks' 2% target into 2024. Meanwhile, China continues to experience slowing inflation.

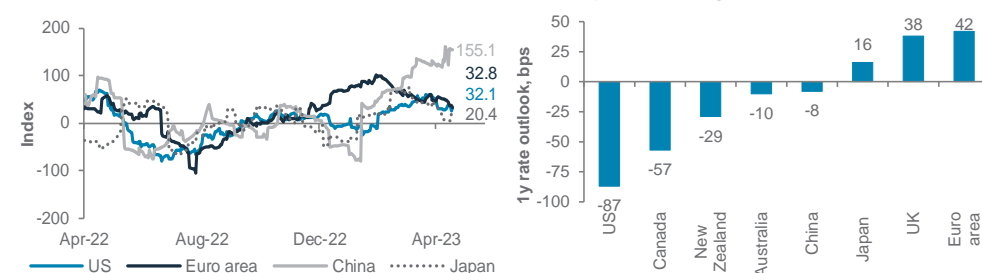
**Policies to diverge:** The divergent global backdrop points to an increasingly divergent monetary policy outlook. We expect the Fed to hike rates by 25bps on 3 May, then briefly pause, before cutting rates in the H2 as a recession likely sets in. Meanwhile, the ECB is likely to hike rates by 50bps in Q2 and hold it there for the rest of the year amid persistent inflation.

## Key chart

*China's economy continues to exceed expectations, while economic surprises in the US and Euro area lose momentum. Against this backdrop, the market is pricing further rate hikes by the ECB and rate cuts by the Fed*

**Fig. 7 China exceeding expectations; US and Euro area have divergent rates outlook**

Citi economic surprise indices; market estimate of policy rate changes over next 12 months



Source: Bloomberg, Standard Chartered

## Macro factors to watch

- US job market, service sector inflation.** The robust job market is the main factor still supporting US consumption and growth. Almost all other indicators in our US recession checklist are signalling a downturn. We expect further deterioration in leading indicators of the job market in the coming months: continuing jobless claims have already risen to a 17-month high, while initial jobless claims are rising y/y; job openings have peaked but remain elevated in historical terms; temporary workers' payroll has started to contract y/y. More weakness in these indicators is likely to cool service sector consumption and inflation and lift the unemployment rate. We expect the Fed to cut rates later this year once the jobless rate starts to rise.
- US debt ceiling risk:** The next 1-3 months are likely to see a rerun of the 2011 battle between the Republicans and the Democrats to raise the US debt ceiling. Only this time, the Republicans (especially a hardliner segment) seem to be more adamant that the debt ceiling cannot be raised without substantial spending cuts. This raises the

risk of a political accident and even a temporary default, given Democrats' firm refusal to negotiate any spending cuts. Thus, **we would categorise this as a "black swan" event risk: low probability, but high temporary impact.** The US has never defaulted on its debt, and a last-minute deal, even if to raise the ceiling for a short period, is likely. However, that could entail large spending cuts. Also, as in 2011, any debt ceiling rise could lead to a brief liquidity shortage as the Treasury boosts borrowing to replenish its cash buffers. The Fed may end its ongoing quantitative tightening plan early to offset this drainage of liquidity.

- China's imbalanced rebound means further stimulus:** The economy's stronger-than-expected 4.5% growth in Q1 was led by domestic consumers, while the manufacturing, private investment and property sectors continued to struggle. Manufacturing is likely to face headwinds as global demand for goods wane (especially with the US likely heading into a recession this year). However, we expect more measures to support the revival of property demand and private investment in the coming months.



# Bonds – at a glance

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Senior Investment Strategist

**Cedric Lam**  
Senior Investment Strategist



## Key themes

**We are Overweight bonds given our expectation of sharply slower US growth.** In our view, US government bond yields are likely to fall (ie, bond prices are likely to rise) as markets price in slower growth, and hence lower policy rates, in the future.

**Our Overweight on DM IG government bonds remains in place.** Slowing growth is likely to mean the Fed pauses after another 25bps hike and starts to cut rates before the end of 2023. This is consistent with our view of falling bond yields, which should help this bond asset class outperform in the next 12 months. Our expected range for the 10-year US government bond yield by end-2023 remains unchanged at 2.75-3.00%. Concern over (i) the US debt ceiling and (ii) the impact on liquidity following the US banking turmoil could keep bond market volatility elevated, but we would use any rebound in yield to add exposure.

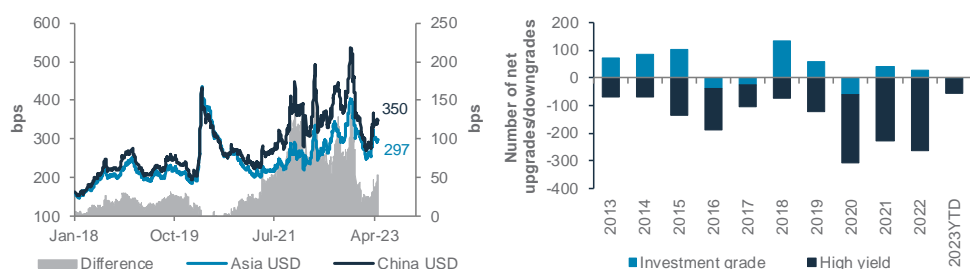
**We remain Overweight on Asia USD bonds, with a relative preference for Investment Grade bonds.** Asia's regional growth should remain supported by China's post-COVID-19 recovery and pro-growth policy initiatives. Although a US recession would pose a risk to this regional economic rebound, we believe Asia USD bond's relatively robust credit quality should act as a buffer.

**We are Neutral on DM IG corporate bonds and Underweight DM HY bonds.** We believe current yield premiums over Treasuries are still insufficient to compensate for a likely forthcoming recession, particularly in HY. **We are Neutral EM local currency (LCY) and EM USD government bonds.** A US recession is likely to be a drag on EM credit quality. However, EM central banks have room to ease policy in need. EM USD bonds should benefit from a high sensitivity to falling US bond yields.

## Key chart

*Widening yield premiums offer an opportunity to add to Asia USD bonds. The case is strongest for IG bonds where credit quality has held up better relative to HY in recent years.*

**Fig. 8 China USD bond yield premium widened relative to Asia USD bonds amid concerns over the longevity of China's recovery; We see a buying opportunity**  
JACI Asia and China yield premiums; Net up/downgrades of Asia IG and HY issuers



Source: Bloomberg, Standard Chartered.

## Should we keep adding into bonds after the yield rally in the past six months?

The 10-year US government bond yield has fallen by c.80bps to 3.45% after peaking in October last year. Despite a decline since March, bond volatility remains high and well above its long-term average. Nevertheless, our expectation of a US recession means we continue to expect yields to move lower to 2.75-3.00% by the end of 2023 as growth slows and the Fed starts to cut before year-end.

Against this backdrop, we continue to see current bond yields as attractive and would use any yield rebounds to add to our preferred bond asset classes.

In addition to the attractive yield itself, we expect investors to benefit from modest capital gains given falling bond yields implies rising bond prices. DM IG government bonds should stand to benefit most from this move. We prefer longer maturity bonds given they are more sensitive to this price impact.

Asia USD bonds are unlikely to gain by the same extent from this sensitivity to US bond yields, given their shorter average maturity profile. However, their higher yield and room for narrowing yield premiums should compensate for this, in our view.

# Equity – at a glance

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## Key themes

We remain **Underweight on global equities** as we expect a recession in the US and Europe to weigh on corporate earnings and equity market returns. The pace of interest rate hikes in the US and Europe will likely tip their economies into recession as central bankers prioritise keeping inflation under control.

We are **Overweight Asia ex-Japan**. China's earnings expectations have been upgraded as its growth outlook improves. In contrast, global equities' earnings have been trimmed as growth slows due to increasingly restrictive monetary policies in the US and Europe. Within Asia ex-Japan, we are **Overweight China equities** due to the government's pro-business stance and with negative sentiment largely priced in. We have an equal preference for onshore and offshore markets. We are **Neutral India equities**, where valuation relative to Asia ex-Japan continues to adjust lower a high, moving closer to the long-term average.

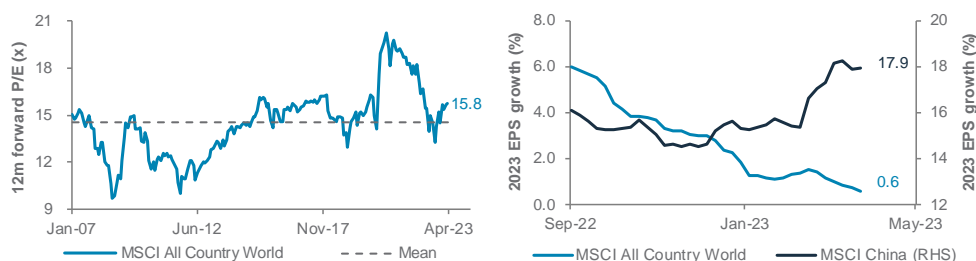
We are **Neutral US equities** where valuation remains elevated and earnings could see weakness if the economy enters a recession. We are **Neutral Euro area equities** where the significant valuation discount is rightly pricing in vulnerabilities to growth. We are **Neutral Japan equities** where benefits from a revival in China's growth are offset by still uncertain monetary policy. We are **Underweight UK equities** where we see the weakest earnings growth this year offsetting its low valuation.

## Key chart

*Valuation for global equities still looks too optimistic to us. Earnings for global equities are under pressure, in contrast to China which is seeing upgrades*

**Fig. 9 Valuation for global equities is above its long-term average and not pricing in risks to a growth slowdown, in our view. 2023 earnings growth for global equities has been revised down since the start of the year but upgraded for China equities**

Consensus 12m forward P/E ratio for MSCI All Country World index. Evolution of consensus 2023 EPS growth for MSCI All Country World and MSCI China over time.



Source: FactSet, Bloomberg, Standard Chartered

## Opportunity in Asia ex-Japan and China

After outperforming strongly at the start of the year, Asia ex-Japan equities have given up the gains and are underperforming global equities YTD. We view this as an opportunity to rotate to Asia ex-Japan, which we continue to believe would outperform over the next 6-12 months.

The key driver for our Asia ex-Japan preference is China, which remains our preferred market within the region. Initial optimism about China's easing of lockdown restrictions appears to have faded. As activity levels normalise in China, some investors question the durability of the growth recovery. On the other hand, some investors are concerned that the strong recovery could prompt the government to dial back on its pro-growth policies. Adding to the negative sentiment are geopolitical concerns as the US seeks to limit investments into high-tech industries in China.

However, we believe the growth outlook in China is improving and this is already supporting positive earnings revisions. Compared with tightening monetary policies in the US and Europe, policies in China remain more supportive of growth. Geopolitical tensions can be expected to continue creating short-term volatility, but we believe this is likely to be offset by business-friendly policies in China as the government seeks high-quality and sustainable growth. In addition, China's valuation remains attractive. We also expect a weaker USD as a tailwind for equities in Asia ex-Japan and China to outperform global equities, as funds flow into the region. In India, earnings delivery continues to be strong. India's 12m forward P/E multiple is off its high, but still a 50% premium to Asia ex-Japan, compared with a historical average premium of 38%.

# FX – at a glance

Abhilash Narayan  
Senior Investment Strategist



## Key themes

**We remain bearish on the USD over the next 3-month and 12-month horizon.** Weakness in US economic data, including some labour market data, and rising concerns around the US debt ceiling showdown have helped push the USD index (DXY) lower since the publication of our Q2 Outlook. We expect a pause in the Fed's rate hiking cycle to lead to less favourable interest rate differentials for the US, pushing the USD lower. US economic slowdown relative to other major economies is likely to reinforce the USD 'Smile' (see the chart below), which should push the USD lower.

**We expect EUR/USD to rise towards 1.12-1.15 over the next three months.** Still elevated inflation, resilient business sentiment and reduced growth downside risks mean that the ECB is likely to maintain its tightening bias, hiking rates by 50bps, with risks skewed to the upside. This should lead to further declines in US vs. German bond yield differentials, pushing EUR/USD higher. However, skewed investor positioning and signs that the EUR could be overbought may lead to a near-term consolidation.

The UK's strong jobs and wage growth and double-digit inflation raise the odds of more rate hikes from the BoE, leading us to **revise our three-month GBP/USD forecast higher to 1.26**. Elevated geopolitical risks and concerns around the US debt ceiling debate could lead to safe-haven demand for the CHF, similar to 2011. Hence, we revise our **three-month USD/CHF forecast lower to 0.90**, with the risk of the pair temporarily edging towards 0.85 should the US debt ceiling showdown turn ugly.

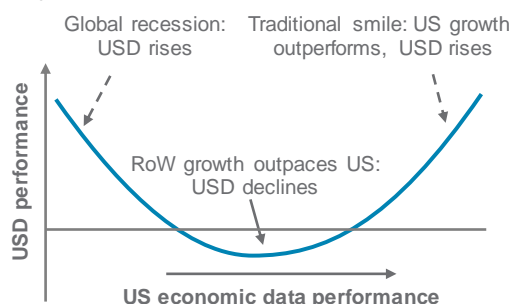
**Commodity currencies (AUD, NZD and CAD) are likely to be supported by China's reopening.** However, the gains could be capped as the RBA and the RBNZ approach the end of their rate hiking cycles. Although the BoJ kept its stance unchanged at its policy meeting in April, we expect gradual progress towards a tightening monetary policy and potential safe-haven demand to push USD/JPY lower from the current level.

## Key chart

*Slower US growth relative to Europe and Asia and US debt ceiling concerns are likely to push the USD lower*

**Fig. 10 US growth and debt ceiling concerns should extend the USD decline**

A stylised representation of USD 'Smile'; Table of forecasts



Source: Bloomberg, Standard Chartered

Currency	3m forecast	12m forecast
USD (DXY)	100.2	99.4
EUR/USD	1.12	1.13
GBP/USD	1.26	1.25
USD/JPY	130	125
AUD/USD	0.68	0.70
NZD/USD	0.63	0.64
USD/CAD	1.34	1.34
USD/CNY	6.83	6.70
USD/CHF	0.90	0.90

## How would USD perform given the looming Fed rate pause and US debt ceiling concerns?

A pause in the Fed's rate hiking cycle is USD bearish in our opinion. While US government bond yields have risen over the past month, we expect the Fed to hike rates in its May FOMC meeting but indicate the likelihood of a pause thereafter. This should help cap 10-year US government bond yields below 3.6%. At the same time, we expect the ECB and BoE to maintain their tightening stance, which is likely to erode the USD's real (net of inflation) yield advantage, pushing it lower. Additionally, an analysis of the past Fed rate hiking cycles suggests that the USD has a tendency to decline in the 3-4 months following the end of a rate hiking cycle, which supports our fundamental view.

Concerns about the US temporarily failing to raise its debt ceiling due to political differences could exert downward pressure on the USD. In the 2011 debt ceiling showdown, the USD fell modestly between May and July of 2011. However, if we take a closer look, the EUR (57% weight in DXY) was rangebound due to the European sovereign debt stress, but the CHF, JPY and gold appreciated vs the USD. Since the Euro area is on a much stronger footing today, we expect the EUR, CHF and JPY to potentially appreciate should US debt ceiling concerns intensify. In this case, **the USD is likely to touch new 2023 lows over the next three months and could even dip below the psychologically important level of 100.**

# Gold, crude oil – at a glance

Zhong Liang Han, CFA  
Investment Strategist



## Key themes

**We remain Overweight gold vs other major asset classes, viewing it as a hedge against tail risk scenarios, with a 12-month forecast of USD 2,100/oz.** Gold has had a strong showing in April, breaking above USD 2,000/oz and staying above this level for most of the month before falling below that level in late April. A weaker USD, continued central bank demand and return of investor interest are key drivers behind its strength, which we expect to sustain. Furthermore, a likely end to the Fed rate-hiking cycle in H1, followed by rate cuts in H2, could propel gold prices to test 2020's all-time high. The precious metal's safe-haven properties also increase its appeal as a diversifier against the backdrop of elevated geopolitical uncertainty.

**We turned more optimistic on oil in the near term, revising our 3-month WTI oil forecast to USD 75/bbl on the back of the surprise OPEC+ output cut.** We expect OPEC+'s move to push the market into a deficit in Q2 vs earlier expectations of a surplus, especially given the strong compliance track record of the participating OPEC+ members in recent times. In the long run, however, we expect WTI oil to trend lower towards USD 65/bbl on (1) weaker oil demand from a slowing global economy, (2) resilience of Russia's exports amid redirection of flows to Asia, and (3) the gradual build-up of inventories from warmer weather. Having said that, any further surprise OPEC+ output cuts are upside risks to our 12-month forecast.

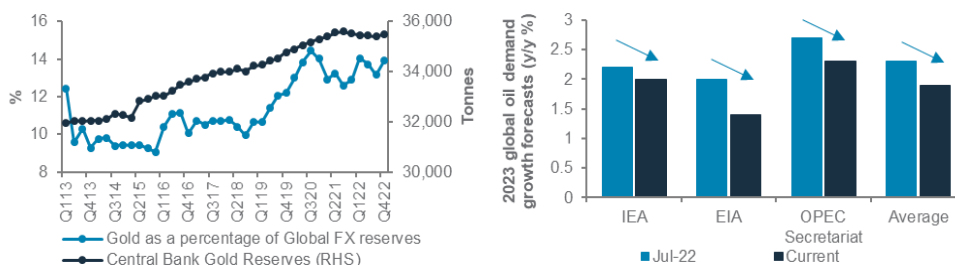
## Key chart

*There is still scope for central banks to further diversify into gold given the still-high allocation to the USD*

*We expect the downward revision of oil demand forecasts to continue as more economic data weaknesses emerge*

**Fig. 11 Global allocation of FX reserves into gold has risen; 2023 oil demand forecasts have fallen over the past nine months**

LHS chart: Central bank gold reserves (tonnes) and as a percentage of FX reserves (%)  
RHS chart: 2023 global oil demand growth forecasts (y/y %)



Source: World Gold Council, Bloomberg, Standard Chartered

## De-dollarisation-led central bank demand

The topic of de-dollarisation is back in focus following the recent headlines around bilateral trades denominated in the CNH and talk of a potential BRICS currency. While we think that the risk of de-dollarisation is overblown, one potential outcome is greater central bank diversification to gold.

Central bank reserves in USD returned to the spotlight following the imposition of US and European sanctions on Russia. That coincided with the acceleration of central bank purchases in 2022. Diversification into gold continued in 2023, largely driven by Singapore, China and Turkey.

Global allocation of FX reserves into gold has risen from 9.4% in 2015 to 14% today. During the same period, gold rose more than 80%. Given that the USD still makes up c.60% of the global reserves, there is still scope for further diversification of the USD into gold.

## OPEC+-led downgrades to demand forecasts

While the consensus is still expecting a y/y increase in oil consumption this year, the forecasts have been on a downtrend over the past year. Relative to mid-2022, 2023 global oil demand y/y growth forecasts have fallen 0.3ppt on average. The declines would have been larger were it not for gains from China's reopening.

In April, the US Energy Information Administration cut its 2023 oil consumption forecast amid the recent banking crisis, while the International Energy Agency maintained its forecast. Although OPEC+ also maintained its forecast, it lowered its estimates for the last three quarters of 2023, while bumping up its Q1 estimate. The large downward revisions likely explain why OPEC+ announced an additional output cut of 1.65mb/d. **We expect demand forecasts to continue falling as more economic data weaknesses emerge.**



# Quant perspective

## US market risk model – remains bearish equities

**Francis Lim**  
Senior Quantitative Strategist

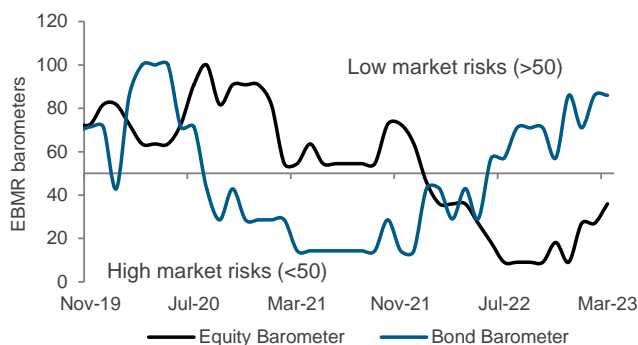
### Model prefers bonds over equities

Our US Equity-Bond Market Risk (EBMR) models the downside risks in US equities and the US 10-year government bonds. It uses 11 economic and market factors to create equity and bond risk barometers. If the value of a barometer falls below 50, it signals higher downside risks and vice versa.

The model continues to suggest we are in Stage 1. This means it expects US equity market risks to remain high, while US government bond market risks to be low. Since the model turned bearish on US equity risks in Jan-2022, VIX has averaged 25pts vs its long-term average of 18pts. The S&P500 index remains 9.0% below its Jan-22 level. The US government 10-year bond yield has increased by 27bp since the model turned bullish on bond market risk in Aug-22. It has previously captured 2.2% rise in US 10-year government bond yield when it was bearish on bond market risks.

**Fig. 12 EBMR bearish on equity and bond market risks**

US equity and bond market risk barometers



Source: Standard Chartered

**Fig. 13 Scenarios over the coming months till July 2023 vs December 2022 projections**

Probability of the evolution of financial market risk cycle from the current Stage 1 and preferred assets

Model's estimated probabilities in December 2022

Stage	Jan-23	Feb-23	Mar-23	Apr-23
1	100%	99%	90%	41%
2	0%	1%	10%	58%
3	0%	0%	0%	1%
4	0%	0%	0%	1%

Model's estimated probabilities in March 2023

Stage	Apr-23	May-23	Jun-23	Jul-23
1	100%	94%	70%	37%
2	0%	5%	28%	59%
3	0%	0%	1%	2%
4	0%	0%	0%	1%

Source: Standard Chartered

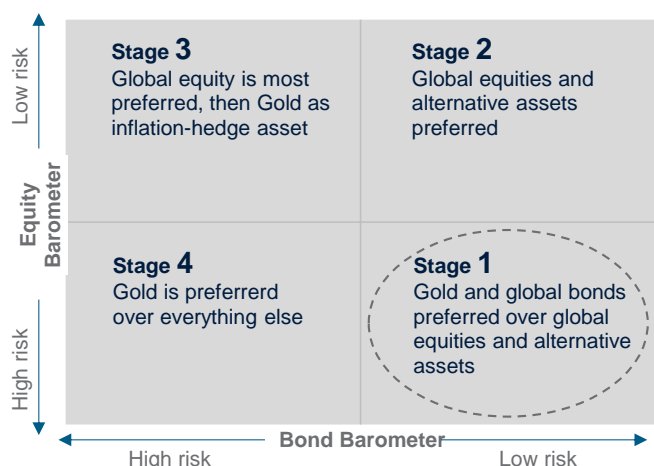
The equity barometer consists of 11 equity indicators. In April, the barometer has so far improved slightly to 36 from 27 and remains bearish (as it is below 50). The improvement is driven by easing inflation, as US CPI ex Food and Energy fell from 6.6% y/y in Sep-22 to 5.6% y/y in Mar-23. Other market factors such as equity and yield momentum have also seen minor improvements, but they remain bearish for risky assets. The theme that continues to underly the bearish equity barometer remains slowing growth, as signalled by falling US housing starts, high interest rates and contracting monetary base.

Our bond barometer remains at a strong 86. Slowing growth remains the supportive factor. This includes ISM manufacturing PMI dropping to 46.3 (a contraction in industrial activity), falling US housing starts and slowing US capacity utilisation. US jobless claims, which was previously a negative factor for the bond barometer, has turned neutral after their recent rise. However, this factor has a bearish bias for our bond barometer as it is still low from a historical perspective. A tight labour market provides more ammunition for rate hike decisions, which are usually bearish for bonds.

Our model projects that the US will remain in Stage 1 until end of June. The model is currently consistent with our GIC views where it sees less downside risks in bonds than equities.

### Implications on global assets

Data since 1999 suggest gold and bonds are the most preferred in Stage 1. The model's preference for an asset is based on its long-term relationship with the market cycle, which favours gold and bonds as defensive assets in Stage 1.



# Tracking market diversity

Francis Lim

Senior Quantitative Strategist

## About our market diversity indicators

Our market diversity indicators help to identify a potential change in short-term trends due to a fall in market breadth across equities, credit, FX and commodities. When market diversity falls, it implies either buyers or sellers are dominating, leading to a rapid rise or fall in asset prices. This is usually unsustainable and is likely to be followed by a slowdown or a reversal. Our diversity indicator is based on a statistical index called fractal dimension; a value below 1.25 serves as a guideline that prices are rising or falling too fast.

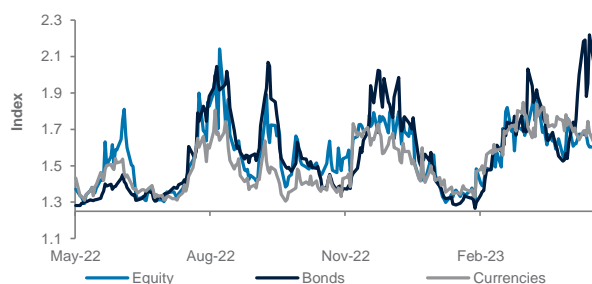
## Where is diversity falling or rising this month?

Market diversity across asset classes we track remain high and none stood out for a reversal trade. This can be seen from Fig. 14, where no assets have a diversity score below 1.25. The diversity of bond markets can be seen to have sharply increased in April.

For bonds, we are seeing a steep rise in diversity, but this is mostly underpinned by stronger price action as investors price in lower probability of rate hikes after the banking crisis. Safer and high-duration bond markets have performed more strongly. For instance, since February, DM government bonds and DM IG corporate bonds have both risen more than 4.0%. The high diversity in these bond markets is positive, as it indicates market positioning is unlikely to cause a reversal.

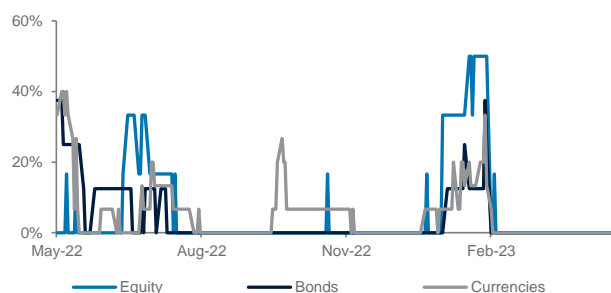
**Fig. 14 Average market diversity score by asset class**

Diversity of bonds has risen steeply



**Fig. 15 Percentage of assets with diversity score <1.25**

No assets showing reversal risks



Source: Bloomberg, Standard Chartered

For equities, market diversity of individual markets has declined but only slightly. The high levels of diversity are driven by market fluctuations where equities had a short-term recovery after the sell-off caused by the banking crisis in March. Overall, a lack of clear market direction will likely keep market diversity of equity markets high. Japan equities currently have the highest level of market diversity, followed by US, UK and Europe ex-UK equities.

Meanwhile, the diversity of currencies has only declined slightly but remains well above our diversity score's threshold of 1.25. This is despite the significant weakness in the USD (DXY down 11% since Sep-22). Any reversal to the current USD weakness is more likely to come from a change in expectations of interest rate differentials. As our diversity score indicates, market positioning does not pose a risk of a reversal in the USD weakness. GBP/USD and EUR/USD currently have the highest market diversity.

**Fig. 16 Diversity across key assets**

Equities	Market diversity	30-day diversity trend
MSCI US	●	→
MSCI Europe	●	↓
MSCI UK	●	↓
MSCI Japan	●	↓
MSCI Asia ex Japan	●	↓
<b>Fixed Income</b>		
DM Government Bonds	●	↑
DM IG Corporate Bonds	●	↑
Global High Yield Bonds	●	↓
EM USD Bonds	●	↓
Asia Credit	●	↑
<b>Commodities</b>		
WTI	●	→

Source: Bloomberg, Standard Chartered; as on 25 April 2023

Legend: ○ Very low ● Low/moderate ● High

# Foundation: Asset allocation summary

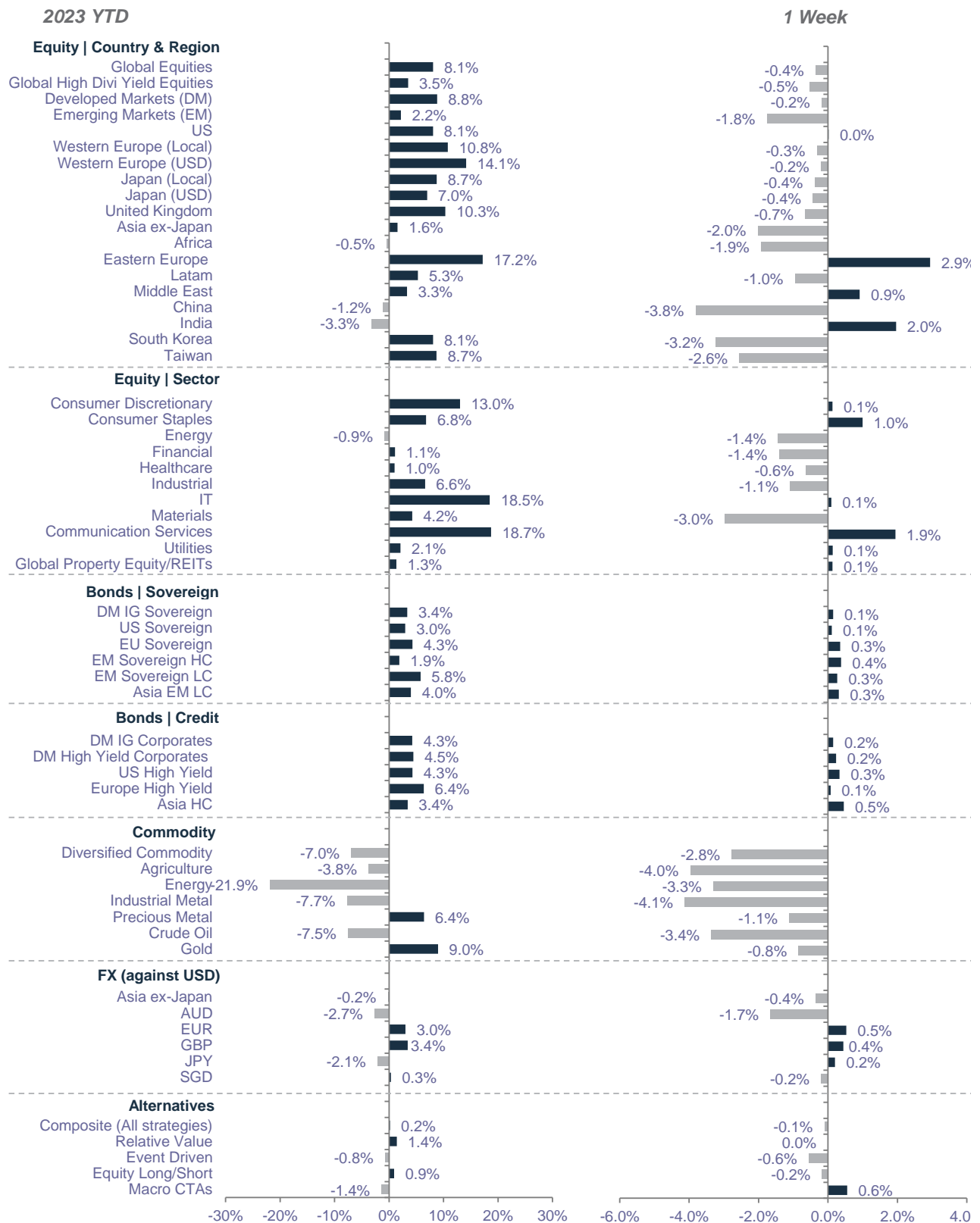
Summary	View	ASIA FOCUSED				GLOBAL FOCUSED			
		Conservative	Moderate	Moderately Aggressive	Aggressive	Conservative	Moderate	Moderately Aggressive	Aggressive
Cash	◆	10	11	6	7	10	11	6	7
Fixed Income	▲	80	54	36	11	80	54	36	11
Equity	▼	6	21	41	70	6	21	41	70
Gold	▲	0	6	7	7	0	6	7	7
Alternatives	◆	4	8	9	5	4	8	9	5
Asset class									
USD Cash	◆	10	11	6	7	10	11	6	7
DM Government Bonds	▲	13	9	6	2	18	12	8	2
DM IG Corporate Bonds	◆	12	8	6	2	17	11	8	2
DM HY Corporate Bonds	▼	7	5	3	1	10	7	4	1
EM USD Government Bonds	◆	14	9	6	2	10	7	5	1
EM Local Ccy Government Bonds	◆	14	9	6	2	10	7	5	1
Asia USD Bonds	▲	20	14	9	3	15	10	7	2
North America Equities	◆	2	7	15	25	3	9	18	30
Europe ex-UK Equities	◆	1	2	4	7	1	3	5	9
UK Equities	▼	0	0	1	1	0	1	1	2
Japan Equities	◆	0	1	2	3	0	1	2	4
Asia ex-Japan Equities	▲	2	8	16	27	2	6	12	21
Non-Asia EM Equities	◆	1	2	4	7	0	2	3	5
Gold	▲	0	6	7	7	0	6	7	7
Alternatives	◆	4	8	9	5	4	8	9	5

Source: Standard Chartered

All figures in %; Allocation figures may not add up to 100 due to rounding.

Legend: ▲ Overweight | ▼ Underweight | ◆ Neutral

# Market performance summary\*



Source: MSCI, JPMorgan, Citigroup, Dow Jones, HFRX, FTSE, Bloomberg, Standard Chartered

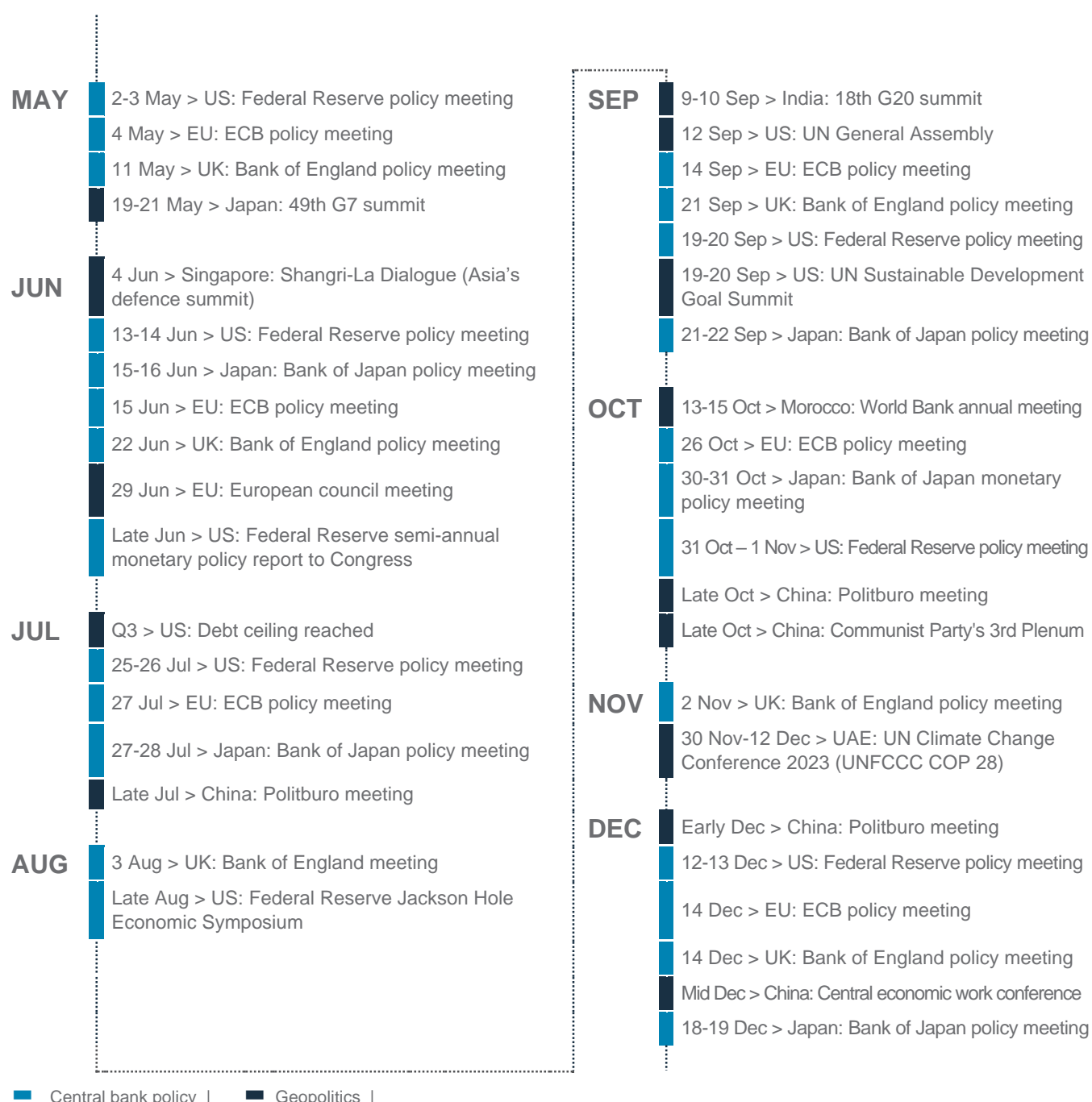
\*All performance shown in USD terms, unless otherwise stated

\*YTD performance data from 31 December 2022 to 27 April 2023 and 1 week-performance from 20 April 2023 to 27 April 2023



# Our key forecasts and calendar events

Currency	USD (DXY)	EUR/USD	GBP/USD	USD/JPY	AUD/USD	NZD/USD	USD/CAD	USD/CNY	USD/CHF	Oil (WTI, USD/bbl)	Gold (USD/oz)	Fed policy rate (upper bound)	US Treasury 10y yield (%)	ECB policy rate
<b>3m forecast</b>	100.2	1.12	1.26	130	0.68	0.63	1.34	6.83	0.90	75	2020	5.25%	3.25-3.50%	3.50%
<b>12m forecast</b>	99.4	1.13	1.25	125	0.70	0.64	1.34	6.70	0.90	65	2100	4.75% (Dec-23)	2.75-3.00%	3.50% (Dec-23)



X – Date not confirmed | ECB – European Central Bank | FOMC – Federal Open Market Committee (US) | BoJ – Bank of Japan | BoE – Bank of England | RBA – Reserve Bank of Australia

# Explanatory notes

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