



Weekly Market View

Is China's recovery sustainable?

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→ We see some durable green shoots: consumer-driven activity is picking up as pent-up demand is met, reviving corporate earnings across services industries.

→ China's overall earnings outlook for 2023 looks much stronger than those for the US and Europe. Also, Beijing continues to provide policy support, in contrast with tightening policy stances in the US and Europe. Moreover, China USD-denominated bond and equity valuations remain inexpensive.

→ We believe the case remains for retaining exposure to China assets within a diversified Asia ex-Japan and global foundation allocation.

What is the reason for the lacklustre performance of the Hang Seng index? What is the outlook?

What is your view on China High Yield bonds and the CNY?

Do you expect the recent weakness in China to have a material impact on commodity prices and currencies?

Charts of the week: Relative value

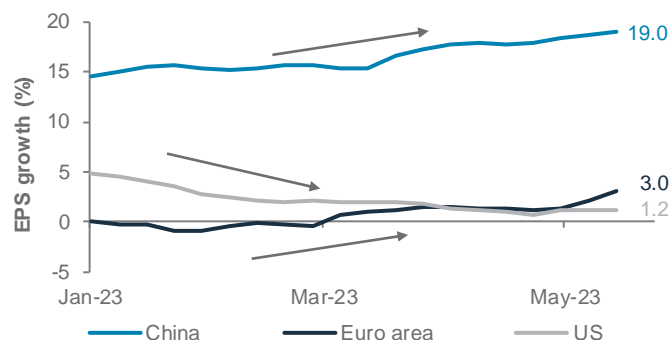
China's consumer demand is improving and corporate earnings estimates are stronger than those in the US and Europe

China's retail sales and new home prices



Source: Bloomberg, Standard Chartered

2023 earnings growth estimates for the US, Euro area, China



Editorial

Is China's recovery sustainable?

China's economic data have underwhelmed lately after a strong start to the year, dragging Asia ex-Japan asset returns. This has also raised doubts about the sustainability of the post-pandemic rebound. We see some durable green shoots: consumer-driven activity is picking up as pent-up demand is met, reviving corporate earnings across services industries. China's overall earnings outlook for 2023 looks much stronger than those for the US and Europe. Also, Beijing continues provide policy support to revive growth, in contrast with tightening policy stances in the US and Europe. Moreover, China USD bond and equity valuations remain inexpensive. We believe the case remains for retaining exposure to China assets within a diversified Asia ex-Japan and global allocation.

Underwhelming April data: China's manufacturing sector and exports remain weak primarily due to a slowdown in economic activity in its main export markets in the US and Europe. Property-related sectors remain under pressure due to structural weakness caused by the overhang of inventory and depressed housing market sentiment. Even retail sales growth fell short of estimates, despite sustaining the y/y growth momentum from last year's low base (see chart above).

Some green shoots: However, we would highlight some encouraging signs that consumers are willing to spend their excess savings accumulated during the pandemic. The latest May "Golden Week" holiday spending exceeded pre-pandemic levels – this is likely to show up in the retail sales data for May. Several regional governments have unveiled incentives to boost consumption of big-ticket items such as cars and consumer durables. Even the depressed housing market is showing some signs of revival as authorities ease mortgage rules to entice first-time buyers. New home sale prices have risen month-on-month for the third straight month. At the latest Politburo meeting, authorities continued to focus on targeted measures to revive growth, jobs, and private investment.

Strong earnings outlook: The post-pandemic revival in the economy is filtering through to strong corporate earnings, especially in consumer-oriented sectors. In Q1, our preferred consumer discretionary and communications services sectors delivered positive earnings surprises, with a strong outlook for the rest of the year. The strong guidance has led to upgrades to 2023 earnings estimates, compared with downgrades to US earnings. Also, China's 2023 earnings estimates remain significantly stronger than those in the US and Europe, primarily due to base effects as the economic reopening lifts revenue.

Attractive valuations: Finally, we believe China's relatively stronger growth and earnings outlook is not reflected in the pricing for its stocks and USD-denominated bonds. Given China's significant weight in Asia ex-Japan and Asia USD bond indices, this undervaluation is also reflected in Asia ex-Japan assets. For instance, the MSCI China equity index is valued at 10.4-times 12-month forward earnings, compared with 18.4x for MSCI US and 12.2x for MSCI Euro area. The MSCI China index is trading at a 34% discount to the MSCI All Country World index, compared with an 18% average discount over the past 20 years. We believe the primary driver for this undervaluation is geopolitics as the US proceeds with measures to curtail access of cutting-edge technology to China. However, we have seen positive overtures lately from the Biden administration to engage with China policymakers for talks. We expect the valuation advantage for China and Asia ex-Japan assets to come to the fore as extreme geopolitical worries subside.

Investment implications: Against this backdrop, we see an opportunity to use the recent weakness in Asia ex-Japan assets to build exposure. We remain overweight on the region's stocks and bonds within our foundation allocations. We are particularly bullish on Asia USD bonds on a 12-month horizon, given the asset class's predominantly investment grade feature and low volatility. Within China equities, the strong Q1 earnings provides us more conviction in the consumer-based equity sectors: consumer discretionary and communications services.

The weekly macro balance sheet

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

(+) factors: US factory output, housing starts; China home sales

(-) factors: China economic activity, hawkish Fed speakers

	Positive for risk assets	Negative for risk assets
Macro data	<ul style="list-style-type: none"> US factory output rose more than expected US housing starts increased unexpectedly China new home prices rose for a third month, but the pace slowed from April Japan economy grew more than expected by 1.6% q/q in Q1, reversing two quarters of contraction 	<ul style="list-style-type: none"> US retail sales rose less than expected by 0.4 m/m US U. of Michigan long-term inflation expectations rose to 12-year high US Empire manufacturing index plunged more than expected, the most since April 2020 US leading indicator deteriorated as expected Euro area factory output fell unexpectedly; growth expectations fell more than expected China retail sales, factory output and fixed assets investment fell short of expectations China property investment contracted unexpectedly
	<p>Our assessment: Negative – Sluggish US retail sales, Euro area growth expectation, rising US long-term inflation expectations, disappointing China economic activity</p>	
Policy developments	<ul style="list-style-type: none"> Fed's Jefferson backed a pause in rate hikes China National Bureau of Statistics called for more efforts to stabilise the housing market China restarted approval on global depositary receipts 	<ul style="list-style-type: none"> Fed's Bullard and Logan said current data did not justify a pause in rate hikes European Commission raised its inflation outlook, citing strong underlying pressures
	<p>Our assessment: Neutral – Fed official comments mixed, China call to stabilise housing market</p>	
Other developments	<ul style="list-style-type: none"> President Biden and McCarthy hopeful of a debt ceiling deal; Biden cut short overseas trip to discuss 	
	<p>Our assessment: Positive – Lower US debt default risk</p>	

Still-resilient US consumption and inflation expectations raise the likelihood of the Fed keeping rates on hold for longer

US core retail sales and Michigan 5-10-year inflation expectations



Source: Bloomberg; Standard Chartered

Euro area growth expectations are faltering

Euro area ZEW survey estimates of economic growth



Source: Bloomberg, Standard Chartered

China's economic data underwhelmed in April, raising the prospects for further policy easing

Economic data surprises indices for the US, Euro area and China



Source: Bloomberg, Standard Chartered

Top client questions

Q What is your view on China High Yield bonds and the CNY, which have continued to weaken?

China High Yield bonds enjoyed a strong rebound in early 2023 on China's initial reopening euphoria. However, more recently, they have underperformed China Investment Grade bonds YTD:

1. The real estate sector remains a large weight in the High Yield asset class. Bottoming sales momentum was a positive, but the recovery remains limited largely to state-backed developers.
2. High Yield bonds are sensitive to economic growth expectations. Recent data disappointments raised some concerns here.
3. The China Q1 recovery has been relatively skewed towards consumption, which has a relatively small asset class weight.

Despite an attractive headline yield, we are not tempted to add exposure due to what we see as a mixed outlook for China HY bonds. We continue to prefer Investment Grade bonds, which we believe offer a better risk/reward today.

USD/CNY broke above the psychologically important threshold of 7.0 this week. This followed weaker-than-expected economic data, leading to renewed expectation of further policy easing, which would shift the interest rate differential against the CNY. We see 7.0425 and 7.1060 as the near-term resistance levels. However, on a longer 6-12 month horizon, we expect the decline in US bond yields to push the pair back below 7.0.

— Cedric Lam, Senior Investment Strategist

— Abhilash Narayan, Senior Investment Strategist

Q What are the reasons for the lacklustre performance of the Hang Seng Index, and what is the outlook?

The Hang Seng Index has been repeatedly testing the key support zone between 19,000-19,500. Following a period of strong economic surprises, Chinese growth data disappointed recently, the latest being fixed asset investment, industrial production and retail sales.

Further targeted and measured policy stimulus is increasingly likely to be needed to boost sentiment and employment and revive private sector business confidence.

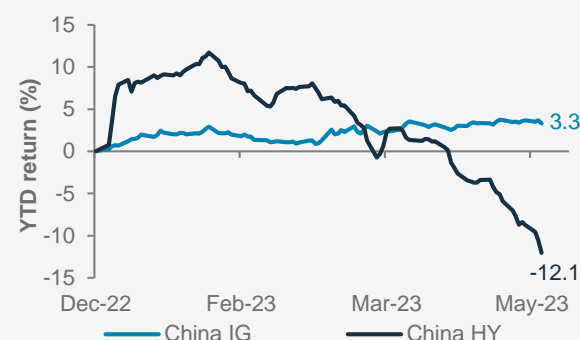
Earnings announcements from internet heavyweights, which began in the second half of this week, could help support the index. Indeed, there have been positive technical signs emerging in the Hang Seng Technology index. For example, its "relative strength indicator" has begun to edge higher, despite the index testing its support level. This shows diminishing strength in the selling of the sector, which we would view as a prelude to a potential recovery.

We continue to like the consumer discretionary and communications services sectors, and would particularly consider accumulating the China internet sub-sector within these.

— Daniel Lam, Head, Equity Strategy

China High Yield bonds have underperformed Investment Grade bonds YTD

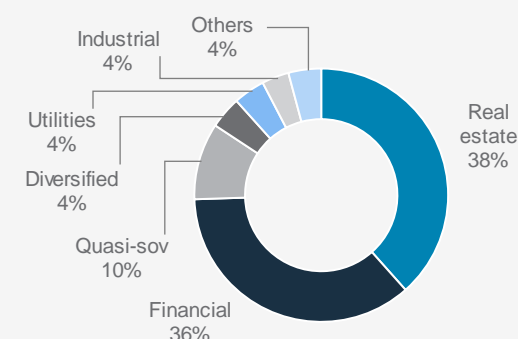
Asian credit index, China IG and HY



Source: Bloomberg, Standard Chartered

The property sector still has a large weight in China High Yield bonds

Breakdown of China High Yield credit index



Source: Bloomberg, Standard Chartered

Hang Seng Index holding support at 19,000

Hang Seng Index



Source: Bloomberg, Standard Chartered

Top client questions (cont'd)

Q Japan equities have been performing very strongly lately. Can this extend?

The MSCI Japan index gained 13% YTD, surging to its highest level since July 1989. Foreign investors have been a key contributor – net buyers of Japanese equity for a 6th consecutive week.

We see the market still being attractively valued in both absolute and relative terms. The MSCI Japan index is trading at a 12-month forward P/E of 14x and a 10% discount to the MSCI All-Country World index, both below their long-term averages. Revised stock exchange corporate governance policies were also likely a support. Share buybacks announced across Japan's firms also rose to an all-time high in FY2023, a trend we expect to last. Japanese equities are relatively less exposed to geopolitical risks than several peers.

While equities have gained YTD, the 10-year Japanese government bond yield has declined. This, combined with the rise in US government bond yields, has led to a more unfavourable interest rate differential for the JPY. We expect US yields to decline and markets to reassess the risk of the BoJ policy shift in light of the strong Q1 GDP growth. We see risks skewed towards lower USDJPY, with 135.75 being a key support.

— Michelle Kam, Investment Strategist
— Abhilash Narayan, Senior Investment Strategist

Q Do you expect the recent weakness in China data to have a material impact on commodity prices and currencies?

Crude oil prices have fallen in recent weeks on the back of disappointing Chinese growth data. China consumes close to 16% of the world's oil production, the second largest after the US. According to the IEA, China also accounted for nearly 60% of global oil demand growth this year. A faltering Chinese economic recovery, thus, would pose downside risk to oil prices. Chinese policy support, however, could mitigate this to some extent. We expect WTI oil prices to remain rangebound in the near term.

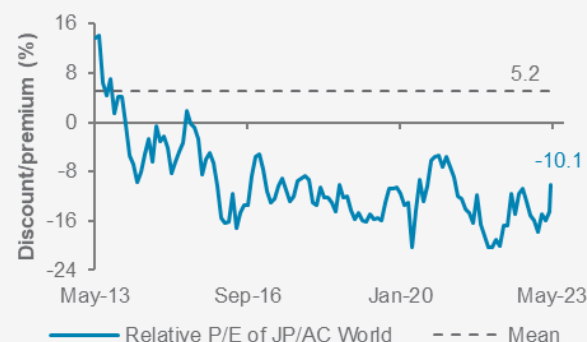
Meanwhile, gold prices benefitted from the soft China data as investors sought a hedge against macro uncertainty. The PBoC also continued to be the second-largest central bank buyer of gold in Q1. We expect these factors to sustain, keeping gold well-supported.

Commodity currencies have had a more mixed reaction to the weaker-than-expected economic data in China. While the AUD weakened and is testing key support levels, the NZD and CAD have largely been resilient. Tactically, we see greater downside risk for the CAD, given the decline in oil prices. However, we do not believe recent data alters our view on commodity currencies as we believe interest rate differentials, rather than commodity prices, are likely to be the dominant driver over the next 6-12 months.

— Zhong Liang Han, CFA, Investment Strategist
— Abhilash Narayan, Senior Investment Strategist

Japan equities are trading at a significant discount relative to global equities

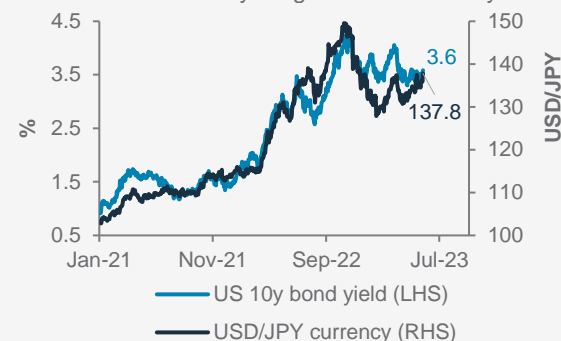
MSCI Japan 12m forward P/E relative to ACWI P/E



Source: FactSet, Standard Chartered

USD/JPY is correlated to US 10-year government bond yields

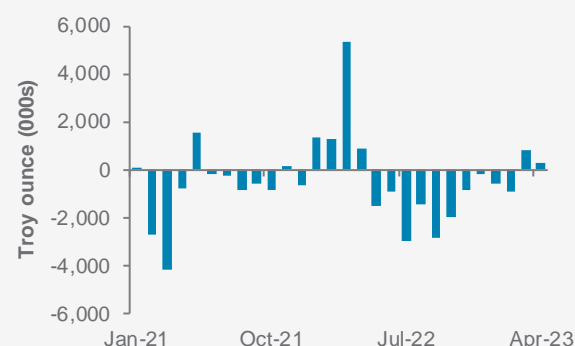
USD/JPY and US 10-year government bond yields



Source: Bloomberg, Standard Chartered

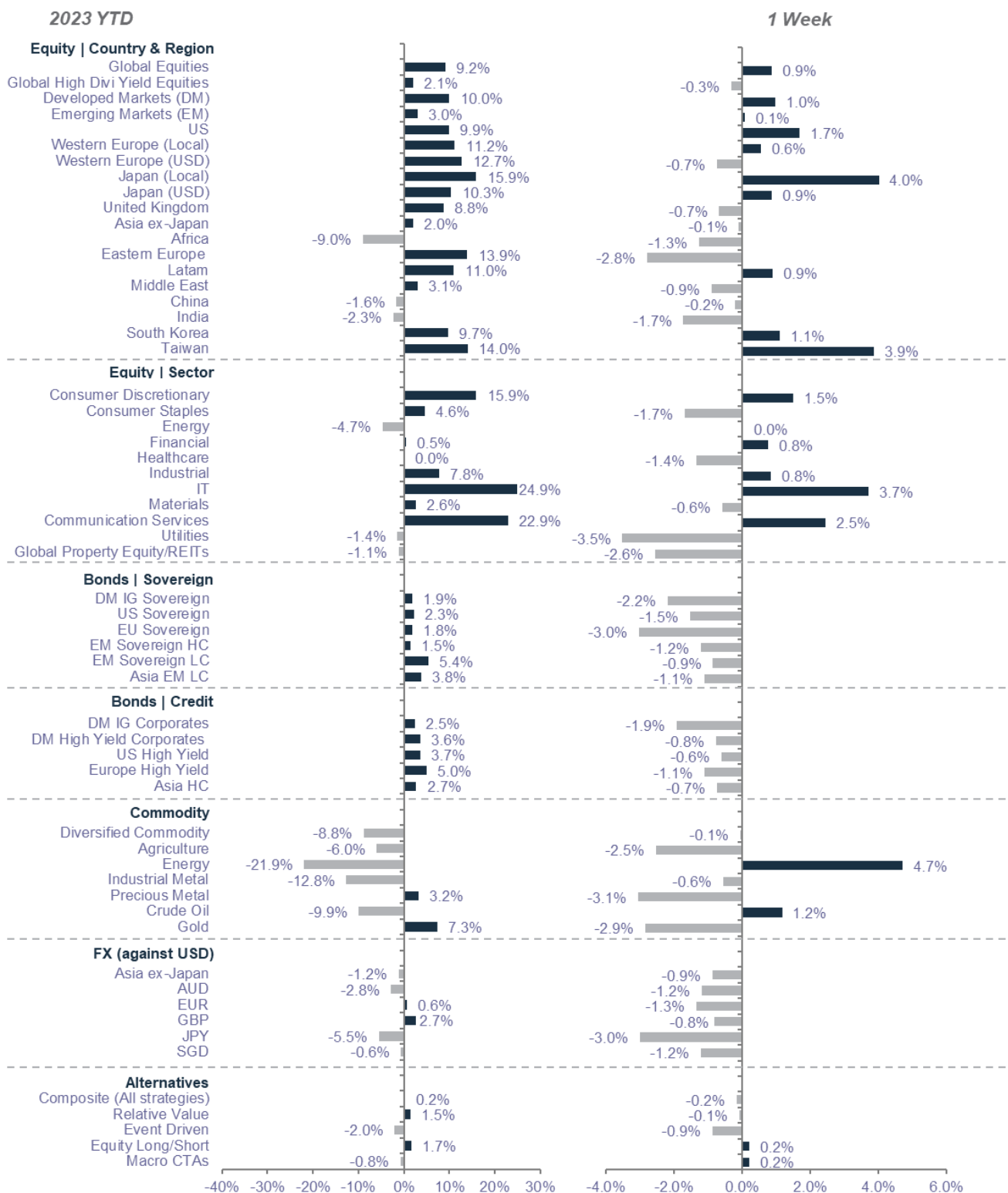
Gold ETFs saw a second consecutive month of inflows in April as investors added to gold

Monthly changes in Gold ETF holdings



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, 2023 YTD performance from 31 December 2022 to 18 May 2023; 1-week period: 11 May 2023 to 18 May 2023

Our 12-month asset class views at a glance

Asset class	
Equities ▼	Preferred Sectors
Euro area ◆	US Healthcare ▲
US ◆	US Staples ▲
UK ▼	US Utilities ▲
Asia ex-Japan ▲	Europe Utilities ▲
Japan ◆	China Discretionary ▲
Other EM ◆	China Comm. Services ▲
	China Technology ▲
	China Industrials ▲
Bonds (Credit) ◆	Alternatives ◆
Asia USD ▲	
Corp DM HY ▼	
Govt EM USD ◆	
Corp DM IG ◆	Gold ▲
Bonds (Govt) ▲	
Govt EM Local ◆	
Govt DM IG ▲	

Source: Standard Chartered Global Investment Committee

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

The US S&P500 index is close to a major resistance

Technical indicators for key markets as of 18 May close

Index	Spot	1st support	1st resistance
S&P 500	4,198	4,139	4,227
STOXX 50	4,367	4,333	4,385
FTSE 100	7,742	7,718	7,772
Nikkei 225	30,749	29,850	31,186
Shanghai Comp	3,297	3,276	3,315
Hang Seng	19,727	19,532	19,950
MSCI Asia ex-Japan	629	626	631
MSCI EM	978	974	981
WTI (Spot)	75.9	74.4	77.2
Gold	1,959	1,939	1,998
UST 10y Yield	3.64	3.52	3.71

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	Consumer Confidence	May P	-16.8	-17.5
	EC	HCOB Eurozone Manufacturing PMI	May P	46.3	45.8
TUE	EC	HCOB Eurozone Services PMI	May P	55.7	56.2
	UK	S&P Global/CIPS UK Manufacturing PMI	May P	–	47.8
	UK	S&P Global/CIPS UK Services PMI	May P	–	55.9
	US	S&P Global US Manufacturing PMI	May P	50.0	50.2
	US	S&P Global US Services PMI	May P	–	53.6
	US	New Home Sales	Apr	660k	683k
	EC	HCOB Eurozone Manufacturing PMI	May P	46.3	45.8
WED	UK	CPI y/y	Apr	8.0%	10.1%
THU	US	FOMC Meeting Minutes	May	–	–
	US	Chicago Fed Nat Activity Index	Apr	–	-0.19
	US	GDP Annualized q/q	1Q S	1.1%	1.1%
FRI/SAT	US	Personal Income	Apr	0.4%	0.3%
	US	PCE Deflator y/y	Apr	–	4.2%
	US	PCE Core Deflator y/y	Apr	4.5%	4.6%
	US	Durable Goods Orders	Apr P	-1.0%	3.2%

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

Investor diversity remains healthy across asset classes

Our proprietary market diversity indicators as of 18 May

Level 1	Diversity	1-month trend	Fractal dimension
Global Bonds	●	↑	1.61
Global Equities	●	↑	2.32
Gold	○	→	1.41
Equity			
MSCI US	●	↑	2.19
MSCI Europe	●	↑	1.76
MSCI AC AXJ	●	↓	1.59
Fixed Income			
DM Corp Bond	●	↑	1.73
DM High Yield	●	↑	2.53
EM USD	●	↑	2.38
EM Local	○	→	1.36
Asia USD	●	↑	2.03
Currencies			
EUR/USD	●	↑	1.64

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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