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Standard Chartered

#pivot?

Outlook 2017

January 2017

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WELCOME TO OUR 2017 OUTLOOK

Not a bad year for investors

As we prepared for this 2017 Outlook, once again our starting point was to look back on the past 12 months to see what happened, what we got right, what we got wrong and what we missed.

In some ways, 2016 was the mirror image of 2015. In 2015, markets were very challenging, but we managed to pick most of the key themes and asset classes that did well to help boost the performance of our model allocations.

This year, markets were much kinder than in 2015. Our multi-asset income approach to investing once again performed well (+8.9%). Meanwhile, oil prices and Emerging Market equities bottomed as we expected and the US dollar remained largely rangebound. However, in hindsight, our decisions to reduce our suggested allocation to global equities in February and again in May were mistakes.

The net result of this is clients are probably happier this year as returns have been much healthier (our tactical asset allocation model for a moderate risk profile shows a return of 7.4% since our 2016 Outlook publication vs -1.7% in 2015).

The key thing we missed was speed of the rise of populism, which crystallised itself in the UK's referendum on European Union membership and the US Presidential election. In hindsight, there was some evidence a year ago of rising dissatisfaction with the status quo, but few (ourselves included) were expecting the shift to be significant enough to deliver such a resounding message of the need for change. The lesson to be learned is that emerging trends can develop much quicker than many anticipate, especially in the world of social media.

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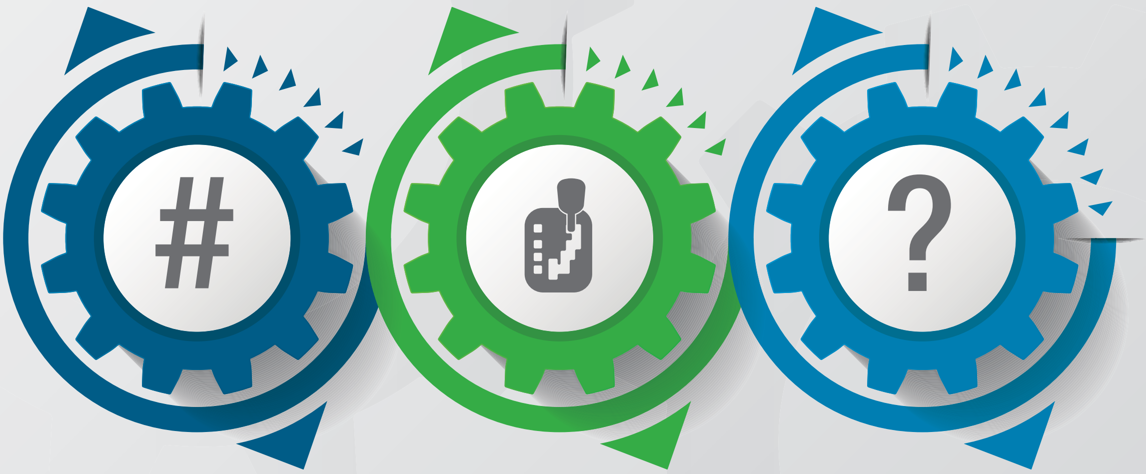


Fast changing world where information/misinformation travels at an ever-increasing speed through cyber-space

Pivot can be defined as ‘keeping one foot firmly grounded while you shift the other in a new direction’

Degree to uncertainty surrounds the magnitude and pace of the pivots

What does this mean for 2017?

Given the uncertainties facing the global economy, we continue to believe it is really important for investors to take into account the possibility of different scenarios when investing (see page 11 for an outline of our main scenarios, including low probability ones). Naturally, these probabilities are as they stand today for the next 6-12 months and are expected to evolve as we move through 2017 and start looking into 2018.

We have tried to capture our thoughts via our '#pivot?' theme. This has 3 aspects to it.

First, the # symbolises a fast changing world where information (and misinformation) travels at an ever-increasing speed through cyber-space, which can accelerate the emergence of trends, both positive and negative.

Second, our preferred definition of pivot is 'to keep one foot firmly grounded while shifting the other in a new direction'. While muddle-through is no longer the dominant central view, it still remains one of two possible scenarios that form our core view (the other being reflationary upside or 'growflation'). We suggest investors keep one foot firmly planted in asset classes that might benefit from a muddle-through scenario while taking a step (pivoting) towards assets that might do well in a reflationary scenario.

Finally, we have included a '?" to highlight the uncertainty regarding the potential pivots, despite the recent market enthusiasm. While in some cases, the direction looks reasonably clear, the magnitude, pace and implications are all open to significant debate and may have been overly priced in, especially in the near term.

For instance, it is not clear what form any US fiscal stimulus will take with some measures likely to find an easier and quicker passage through the legislature than others. Finally, it is easy to assume that, in a growth-starved world, a fiscal stimulus is a positive development. However, with the US already approaching full capacity, it is quite possible that increased government spending and tax cuts feed through to more inflation rather than faster growth.

There has been a very fast shift in sentiment towards a reflationary scenario in recent times. A continuation of this momentum is contingent on fiscal policies being implemented that would support this scenario. While initial signs look promising, we highlight it is early in the game. It is still unclear whether this pivot towards reflation is a sustainable trend and, even if it is, we doubt it will be a smooth process.

This leads us to recommend clients to keep a diversified allocation, with the majority focused on the muddle-through and growflation scenarios, albeit with some hedges on the tail risks, particularly in the area of accelerating inflation (see page 27).

This publication aims to be a map for 2017 that helps you navigate through uncharted waters in 2017. As always, we will provide regular updates as we go through the year on emerging opportunities and risks.

What you should do

We highly recommend that you reach out to your relationship manager to understand fully the implications of our views for you and to consider whether any changes to your investment allocations are warranted.

Meanwhile, I wish everybody a very Happy New Year and all the best in the year ahead.

[Alexis Calla]

2017: THE YEAR OF THE #PIVOT?

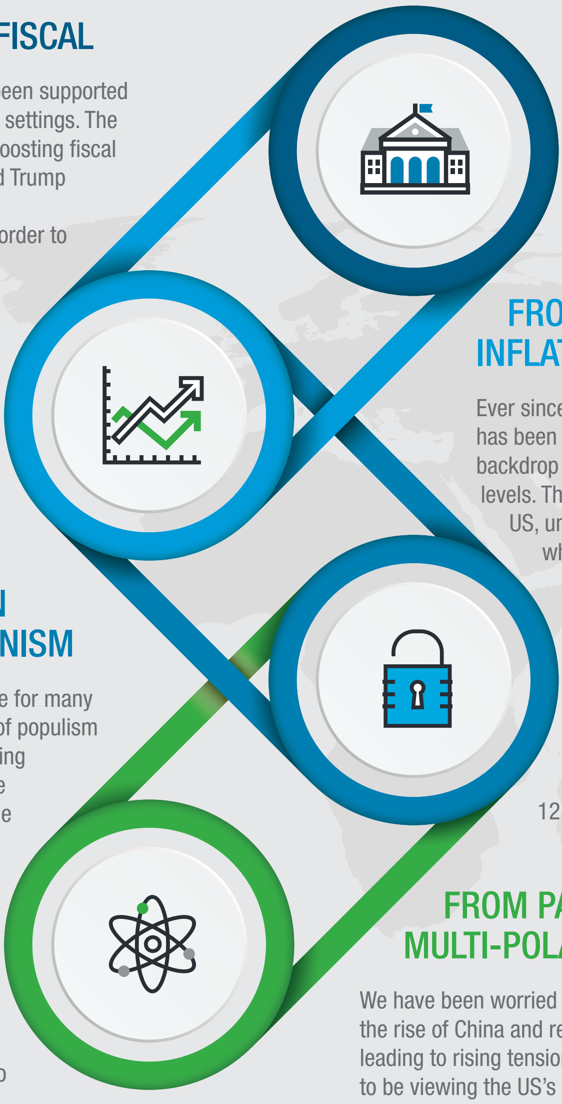
[Steve Brice]

Financial markets have moved rapidly since the US election in the belief that 2017 will shape up to be a pivotal year.

We agree that global economic confidence has been boosted by increased expectations of faster growth and inflation, possibly ending years of a deflationary mindset. Some examples of expected changes (or pivots) to the global economic and financial landscape that we see evolving in 2017 are highlighted below. However, we would take a more balanced view as we are not convinced these shifts will be as seismic as many expect.

FROM MONETARY TO FISCAL

Ever since 1999, economies have been supported by extremely loose monetary policy settings. The US is now taking a leading role in boosting fiscal policies with President-elect Donald Trump arguing for tax cuts and increased infrastructure/defence spending in order to spur economic activity. This should cause the Fed to gradually tighten monetary policy.



FROM DEFLATION TO INFLATION

Ever since the Global Financial Crisis, the focus has been on deflationary fears against the backdrop of sluggish growth and very high debt levels. This may be coming to an end. In the US, unemployment is already at levels which usually trigger accelerating wages. Meanwhile, after declining for almost 5 years, Chinese producer prices have started rising modestly, removing another large disinflationary force. Finally, rising oil prices are expected to contribute to gradually rising inflationary pressures in the coming 12 months.

FROM GLOBALISATION TOWARDS PROTECTIONISM

Globalisation has been a key feature for many decades. The dramatic expression of populism over the past 12 months risks a swing towards a more protectionist stance against global trade. The US is at the forefront of this shift. For now, the US has merely called a halt to further globalisation rather than embarking on protectionist measures, with the Trans-Pacific Partnership (TPP) the main casualty. The risk of protectionist measures is rising, although for now we expect them to be targeted.

FROM PAX AMERICANA TO MULTI-POLARITY

We have been worried about this theme for some time with the rise of China and relative decline of the US likely leading to rising tensions, especially in Asia. China appears to be viewing the US's decision to pull out of the TPP as an opportunity to expand its sphere of influence. This infers a potential Asian pivot away from the US towards China. History teaches us that multi-polarity can often lead to extreme 'black swan' events.

Implications for investors

Of course, there is still much uncertainty in the world, including how long the above pivots will last, how quickly they will happen and what the implications will be. However, we still see this pivot lens as a useful one for investors to bear in mind when making investment decisions.

Thus far, markets are clearly focusing more on the positive aspects of the reflation pivot. Equities have rallied, led by Developed Markets, bond yields have risen and the US dollar has rallied.

Stronger global economic growth in 2017, which would be only the second global acceleration since 2009, a modest rise in inflation and corporate tax cuts should benefit equities, especially in the US. Meanwhile, a weaker JPY should boost Japan corporate profitability, increasing the attractiveness of Japanese equities on a currency-hedged basis. US dollar strength and fears over protectionism have proven to be a headwind for Emerging Market equities (see pages 47-57 for our key equity views, and pages 58-63 for our currency outlook).

Within bonds, the rising inflationary pressures suggest we would look for opportunities to reduce our exposure and shorten our maturity profile. Our favoured spaces within bonds are US high yield – due to its higher yields, lower interest rate sensitivity, exposure to rising oil prices and potential for corporate credit quality to improve should the economy recover – and US leveraged loans – due to their exposure to rising interest rates (see pages 40-46 for our key bond calls).

Finally, we still believe the highly successful multi-asset income strategy is appropriate for income investors to the extent that we believe it can generate a sustainable 4-5% yield. However, we have less confidence that it will outperform a multi-asset growth allocation as it did these recent years. Therefore, we selectively identify growth areas that we believe should be added for 2017 (see pages 24-39 for our views on multi-asset investing).

However, as highlighted above, nothing is certain in this world. Exactly what policies will be implemented is still unknown. For instance, if the US government focuses on tax cuts for the rich, the economic impact is likely to be lower than an increase in infrastructure spending. Meanwhile, it is quite possible that inflation, which was already expected to rise slightly, will rise more dramatically. This could push up interest rates and yields more swiftly, undermining equities.

Given these uncertainties, which will only increase as the economic recovery extends, we believe investors will find useful a scenario-based approach to investing, which naturally results in a balanced investment profile. This should include some hedges against a less favourable scenario the markets are currently pricing in, especially with regards to the risk of higher inflation (see pages 69-70 for our views on alternative strategies). The table below summarises our preferred asset classes as we head into 2017.

KEY INVESTMENT VIEWS

MULTI-ASSET

Multi-asset income allocation to deliver positive absolute returns

Balanced allocation (mix of 50% Global Equity & 50% Global Fixed Income) to outperform multi-asset income allocation

BONDS

Corporate bonds to outperform government bonds

DM High Yield bonds to outperform broader bond universe

US floating rate senior loans to deliver positive returns

EQUITIES

US, Japan (FX-hedged) to outperform global equities

India, Indonesia to outperform within Asia ex-Japan

COMMODITIES

Brent crude oil price to be higher by end 2017

ALTERNATIVE STRATEGIES

Our alternative strategies allocation to deliver positive absolute returns in 2017

FX

EUR/USD to fall

AUD/USD to rise

USD/CNY to rise

MACRO OVERVIEW
AT A GLANCE

[Rajat Bhattacharya]

KEY THEMES

Global growth is likely to accelerate in 2017 for only the second year since the financial crisis, as Russia and Brazil emerge from two years of recession and as US growth accelerates modestly. Asia, including China, is likely to remain the biggest contributor of global growth.

Deflationary pressures are fading. We expect an upturn in inflation worldwide, especially in the US, as tightening labour markets fuel wage pressures and amid a recovery in oil and commodity prices.

Policy focus in the Developed Markets to shift from monetary to fiscal measures to revive growth and inflation. Donald Trump's election in the US has raised expectation of a strong fiscal stimulus package. Monetary policy is likely to remain accommodative across major economies.

The key alternative scenarios, we believe, are three-fold: 1) Continuation of muddle-through growth as a result of a sharp rise in bond yields/rates and a stronger USD. **2)** Stagflation, or a sharp upturn in inflation caused by reflationary policies, without generating any growth upsurge. **3)** Return to deflation.

KEY DRIVERS

Region	Growth	Inflation	Benchmark Rates	Fiscal Deficit	Comments
US	▲	▲	▲	▲	Growth to get a boost from fiscal stimulus. Risk of more than two expected Fed hikes if inflation accelerates
Euro Area	▼	▲	◗	◗	Growth and inflation to stay lacklustre. ECB to continue stimulus. Watch political risks
UK	▼	▲	◗	◗	Growth to falter amid Brexit uncertainty. BoE may tolerate inflation up to c. 3%
Japan	▲	▲	◗	◗	JPY weakness to support export-led growth. More fiscal easing likely as BoJ anchors long-term yields
Asia ex-Japan	◗	◗	◗	◗	China to provide stability ahead of key Party Congress. US trade policy key risk for region
Emerging Markets ex-Asia	▲	▼	▼	▼	Brazil, Russia to emerge from recession, helped by commodity prices. US policy clouds Mexico

Source: Bloomberg (based on consensus estimates for 2017), Standard Chartered
Legend: ▲ Higher growth/inflation/benchmark rates/fiscal deficit | ▼ Lower growth/inflation/benchmark rates/fiscal deficit | ◗ Little change

KEY CHART

The US is likely to provide the biggest lift to global growth among Developed Markets, while Brazil and Russia are likely to provide the biggest boost within Emerging Markets

	GDP (%)		CPI (%)		Budget (% of GDP)			Key Rates (%)	
	2016	2017	2016	2017	2015	2016	2017	2016	2017
United States	1.60	2.20	1.30	2.30	-2.60	-3.20	-3.20	0.75	1.25
Eurozone	1.60	1.30	0.20	1.30	-2.10	-1.90	-1.70	0.00	0.00
China	6.70	6.40	2.00	2.10	-3.40	-3.10	-3.50	4.35	4.20
Japan	0.60	0.80	-0.20	0.50	-6.70	-5.80	-5.30	0.00	-0.10
United Kingdom	2.00	1.00	0.70	2.40	-4.30	-3.70	-3.50	0.25	0.25
India	7.30	7.60	4.80	5.00	-3.50	-3.50	-3.30	6.25	6.00
Brazil	-3.30	1.00	8.70	5.40	-8.20	-9.10	-8.90	13.75	10.75
Canada	1.30	1.80	1.50	1.90	0.10	-1.30	-1.50	0.50	0.50
South Korea	2.70	2.60	1.00	1.70	0.00	0.10	0.30	1.25	1.05
Australia	2.90	2.70	1.30	2.00	-1.90	-2.40	-2.00	1.50	1.35
Russia	-0.60	1.30	7.10	5.20	-2.80	-3.80	-3.00	10.00	8.25
Mexico	2.10	1.80	2.80	3.70	-3.50	-3.00	-2.50	5.50	6.10

Source: Bloomberg consensus forecasts for the world's top 12 economies; Standard Chartered

FROM MUDDLE-THROUGH TO REFLATION?

Core scenarios

The world economy stands at a crossroads. One path leads to a controlled recovery in growth and inflation, with the help of reflationary policies pursued by governments and central banks (i.e. the **reflationary upside** scenario). The other path would see the world continuing to **muddle-through** in an environment of structurally slow growth and low inflation that has persisted since the Global Financial Crisis.

At this juncture, our Global Investment Committee (GIC) places almost equal probability to these two scenarios, the deciding factor being the size of budgetary stimulus Developed Market governments (especially in the US) are able to implement to boost growth and productivity in their economies. This is quite a turnaround from a year ago, when the world struggled to emerge from a deflationary scare, relying on domestic consumers to generate mediocre growth.

The recovery theme comes with its own risks: first, there is a chance that the reflationary policies – enacted at a time when labour markets in some major economies (particularly in the US) are already tight – could lead to acceleration in inflation, but without generating significant growth (the **stagflation** scenario). Reflationary policies are also likely to fuel ongoing recovery in commodity prices, increasing so-called 'stagflation' risks. The USD's recent strength should be disinflationary, but may not be sufficient to stall the uptrend in wages.

The other scenario, which we believe is the least likely, is a descent into full-blown **deflation**. One possible cause would be a flare-up in Euro area tensions, possibly from the rise of populist parties in elections next year or from any significant banking sector instability. Thus, the focus is likely to remain on the Brexit talks, progress of Italy's bank recapitalisation and upcoming elections in France and Germany. Another catalyst could be a rise in protectionist policies. See page 27 for asset classes we would expect to do well in the different scenarios.

Figure 1: Reflation and muddle-through scenarios are seen as most likely, with stagflation and deflation scenarios remaining outside risks

Four key scenarios and probability assigned by Global Investment Committee to each

Source: Standard Chartered Global Investment Committee

Global outlook improves on easier fiscal policies

The global outlook is constructive at the time of going to print. Consensus forecasts show global growth is expected to accelerate to 3.2% in 2017, from an estimated 2.9% in 2016. That would make it only the second such instance of year-on-year acceleration since the Global Financial Crisis.

Some emerging economies are likely to lead this turnaround as Brazil and Russia return to growth after a couple of years of recession, aided by a recovery in commodity prices from multi-decade lows. In this base reflationary scenario, China's fiscal and credit stimulus – implemented over the past couple of years – continues to provide stability for Emerging Markets, besides sustaining the recovery in commodity prices. Asia is likely to contribute 60% of global growth in 2017.

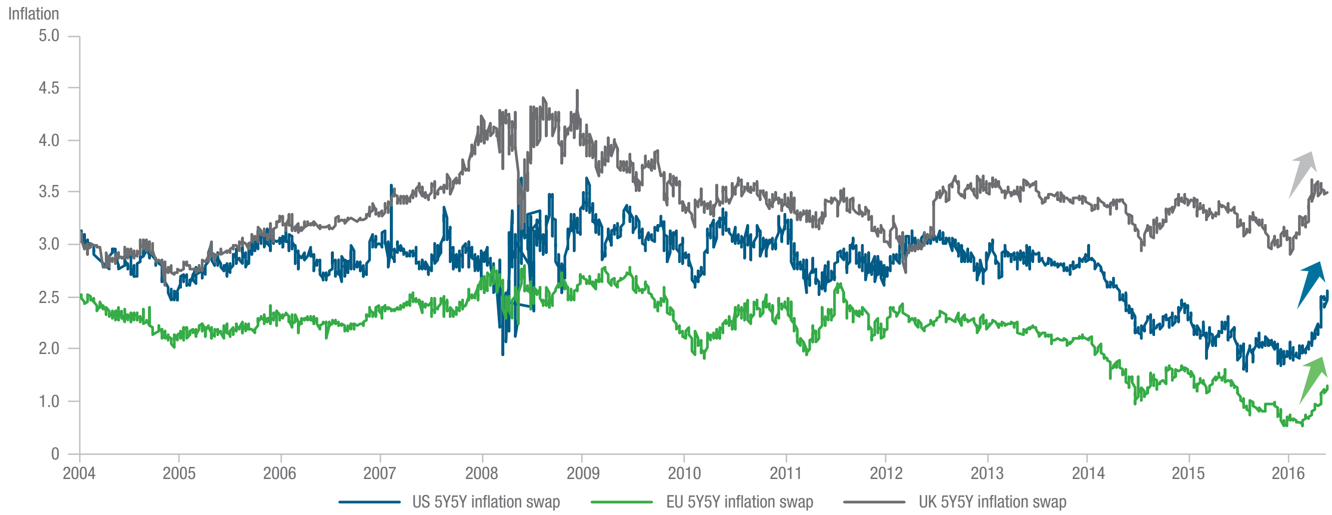
Fiscal policy in the Developed Markets has the potential to positively lift global growth. This is especially important as monetary policy remains supportive (and real interest rates negative), even with the Fed likely raising benchmark rates by around 50bps over the next 12 months. We expect the ECB, BoJ and PBoC to maintain their already accommodative monetary policies through 2017.

Fiscal policy has already started to ease in several economies – the US fiscal deficit rose in 2016 for the first time since 2009. Further easing as a result of simplification of tax policies (or cutting taxes) and higher spending on infrastructure could lift US growth above recent trend of around 2%. However, this risks stoking inflation, forcing the Fed to raise rates a lot faster than the expected two hikes and boosting the USD. Higher rates and stronger USD could act as powerful brakes in this scenario.

New governments in the UK and Canada have abandoned earlier plans to achieve budget surpluses and have instead proposed tax cuts and higher infrastructure spending. Meanwhile, Japan's policy of controlling long-term government bond yields is likely to enable the government to sell long-term bonds to finance infrastructure spending, while a weaker JPY helps its exporters. China, which started implementing its fiscal boost two years ago, is likely to maintain its stimulus as it stabilises growth in the run-up to the crucial, once-in-five-years, Communist Party Congress in Q4 2017 (which will select the next batch of leaders). Only Europe appears to be refraining from expanding fiscal policy either due to political reluctance (Germany) or perceived financial constraints (in southern Europe).

Figure 2: Inflation expectations are rising amid tighter labour markets and higher commodity prices

Long-term market-based inflation expectations in the US, UK and the Euro area (5-year, 5-year inflation swap rates)



Source: Bloomberg, Standard Chartered

US: Going fiscal

1. US economy to see an eighth year of expansion, with consumption and business investment accelerating on the back of easier fiscal policies
2. We expect President-elect Trump to at least partially deliver on his promise to cut taxes, ease business regulations and boost spending on infrastructure, helping lengthen an already-extended business cycle
3. The key risk is a sharp rise in inflation as Trump's stimulus measures accentuate an already tight job market, fuelling wage pressures. This could lift yields higher and boost the USD, eventually dampening growth
4. The Fed is likely to hike rates at least twice in 2017 as inflationary pressures start to build, but a strong US dollar means further rate rises are likely to be gradual

Trump's policy priorities

The impact of the US Presidential election is debatable, but one issue which both sides agreed on in the run-up to the polls was the use of fiscal policy tools, including the need for more investment in infrastructure to boost growth and productivity. Markets have priced in growth-supportive policies, which implies expectations have been set high for 2017-2018.

In his first public statement since the election, President-elect Trump highlighted several policy priorities, all of which are focused on boosting US manufacturing and jobs. These include: abandoning the Trans-Pacific Partnership trade agreement (which the US was due to sign with 11 other Pacific-rim economies such as Japan, Australia, Canada, Mexico); relaxing environmental restrictions on the energy sector to revive the domestic shale oil and gas and clean-coal sectors; easing business regulations (especially related to banks); boosting infrastructure and defence spending (including cyber-security); and tightening immigration rules.

The US economic outlook is likely to depend significantly on how a Trump administration prioritises these policies. For instance, a focus on trade disputes in the early stages (including punitive tariffs on China and other trade partners pledged during the election campaign) could be negative for growth and may fuel inflationary pressures. Similarly, tougher immigration policies could impact critical sectors including construction, energy and retail industries.

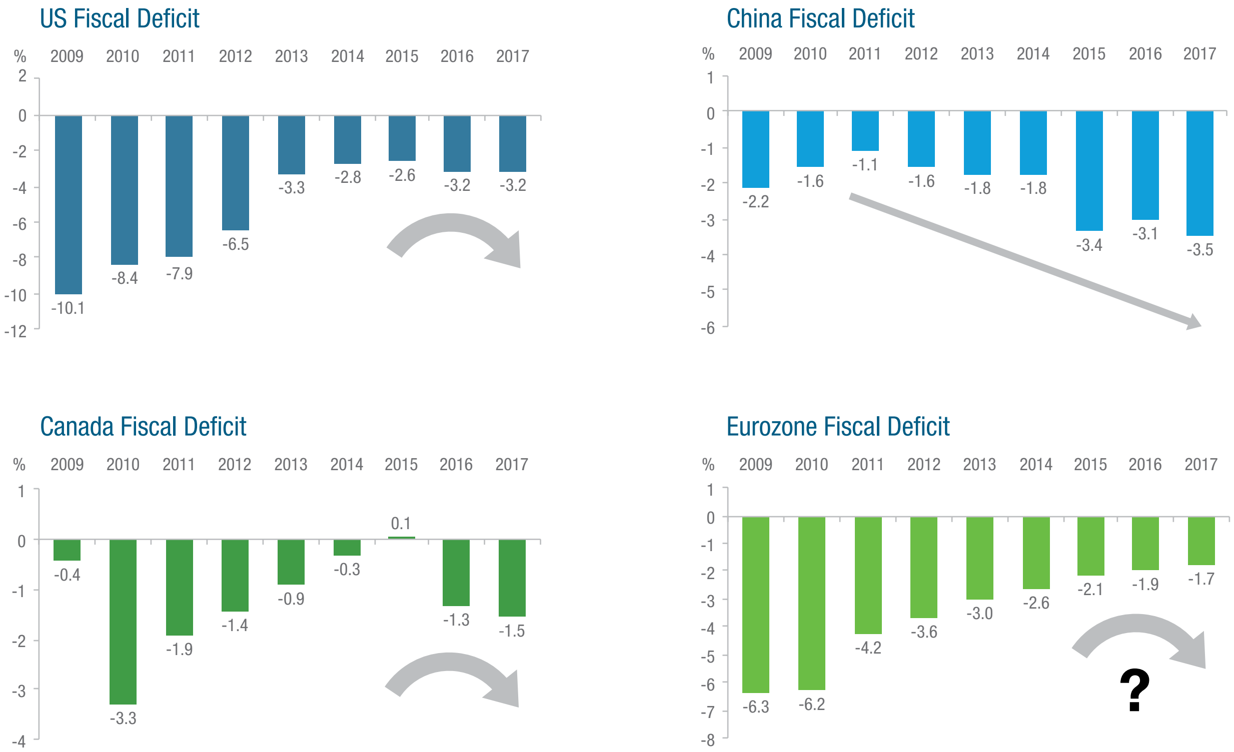
The Republicans control over both houses of Congress is likely to help the Trump administration push through many of its policy priorities. However, our base case is that the new administration will initially focus on areas where there is broader consensus among both parties. These include revamping tax laws, lowering corporate and personal taxes, incentivising companies to repatriate overseas-held cash and invest in the US; and implementing a plan to boost infrastructure-spending (Trump's campaign noted a USD1 trillion infrastructure spending gap over 10 years).

How the incoming administration chooses to fund the proposed tax cuts and infrastructure investments is likely to have a significant impact on financial markets. Trump has pledged a deficit-neutral plan. Any slippage is likely to boost borrowing costs.

Overall, we expect US economic activity to pick-up on the back of sustained consumption as the job market remains robust and wages continue to accelerate. Proposed personal tax cuts are likely to further boost consumption, while corporate tax cuts are expected to help revive business investment at least to some degree, improving productivity over the longer term. The housing market is expected to remain a growth engine as pent-up demand for residential housing stays high amid a continued recovery in the job market. However, the recent rebound in long-term interest rates risks increasing mortgage costs, potentially thwarting the sector's expansion.

Figure 3: China led the easing of fiscal policy since 2012; US and Canada are likely to follow, reversing years of budget tightening

US, China, Canada and Euro area fiscal deficit (% of GDP); 2016 and 2017 figures are Bloomberg consensus estimates



Source: Bloomberg, Standard Chartered

Monitoring inflation

We will also monitor the implications of Trump's policies on inflation. Long-term inflation expectations have picked up significantly since the election victory, partly on expectations that a fiscal stimulus and tougher immigration policies at a time when unemployment is close to the Fed's optimal target could lead to higher wage pressures. Thus, a stronger upsurge in inflation, driven by supply constraints, remains a key risk for the US economic outlook, although it is important to note that the relationship between wages and inflation is not clear-cut.

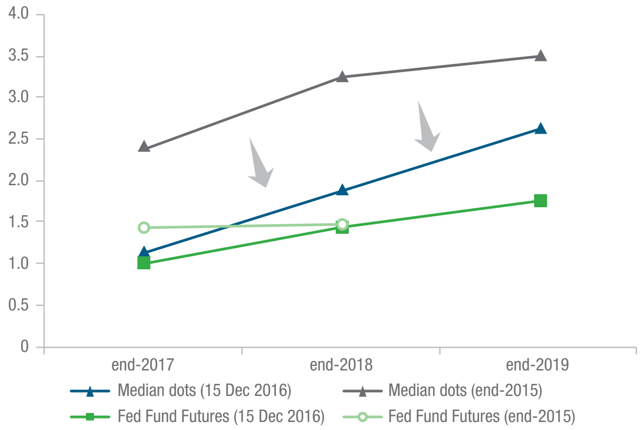
There may be sufficient 'hidden' labour market slack, given the low job market participation rates and still high levels of part-time workers, to absorb increased demand for workers as infrastructure projects are implemented over the next few years.

Hawkish Fed?

Thus, we believe, the Fed is likely to raise rates at least twice in 2017. However, changes (by member rotation) to the Fed's policy rate-setting committee in 2017 are expected to bring in more members to the board who are biased towards raising rates. The Trump administration is also likely to nominate at least two members to the Fed's board – which could bring a slightly more hawkish bias. Thus, as with inflation, the risk to US interest rates in 2017 is on the upside.

Figure 4: Fed estimates of rate hikes have moved closer to market expectations in 2016

Market estimates of Fed rate hikes based on Fed funds futures; Fed estimates of rate hikes (median dots)



Source: Bloomberg, Standard Chartered

Europe: Politics in focus

1. Euro area growth is likely to slow in 2017 as political uncertainty and excess capacity hold back business investment, offsetting a likely boost to exports from a weak EUR. The UK faces Brexit-related uncertainty
2. Inflation expectations are rising across Europe on higher commodity prices, particularly in the UK because of the sharp devaluation in the GBP. However, Euro area inflation remains well below the ECB's 2% target
3. The biggest risk to the region is a rise in populist or anti-establishment parties in the upcoming elections. The UK faces the risk of a 'hard-Brexit' if Euro area policymakers deny it open access to its common market
4. The ECB is likely to maintain stimulus as inflation stays below target. The BoE is likely to tolerate a rise in inflation above its 2% target to support growth. However, inflation above 3% may increase pressure to raise rates

Election watch

While the US economy has the potential to deliver an upside surprise, the Euro area carries negative risks. The main uncertainty originates from its busy political calendar next year. Italy's referendum, wherein voters rejected the government's reform proposal leading to the resignation of Prime Minister Matteo Renzi, highlights the potential risks from elections in France, the Netherlands and Germany in 2017.

German Chancellor Angela Merkel's decision to run for a fourth term and Austria rejecting a right-wing party this month are positive for Euro area political stability and continuity in policies. However, the prospect of France's far-right candidate, Marine Le Pen, proceeding to the final round of the French presidential elections may raise concerns about another electoral upset similar to the Brexit vote and Trump's win in the US. While Le Pen is significantly trailing the Republican candidate in opinion polls, investors will have learned to be sceptical of such polls over the past 12 months, especially so many months before elections.

For now, data suggests the Euro area economy has weathered the post-Brexit slowdown. Business and investor confidence indicators have recovered from their Q3 slump. The weaker EUR continues to support exports, and could yet help Euro area growth surprise on the upside, while record low borrowing costs are helping consumers and businesses.

Accommodative ECB

Excess capacity persists both in manufacturing and labour markets, the latter caused by still-high unemployment rates in southern Europe. This remains a challenge as it continues to dampen inflation expectations. While producer price deflation appears to be receding (aided by a recovery in oil prices) and consumer prices have started to rise again, inflation remains well below the ECB's 2% target. The ECB acknowledged the risk as it extended its bond purchase plan until the end of 2017, while reducing the amount of bonds it would buy each month.

UK: Preparing for Brexit

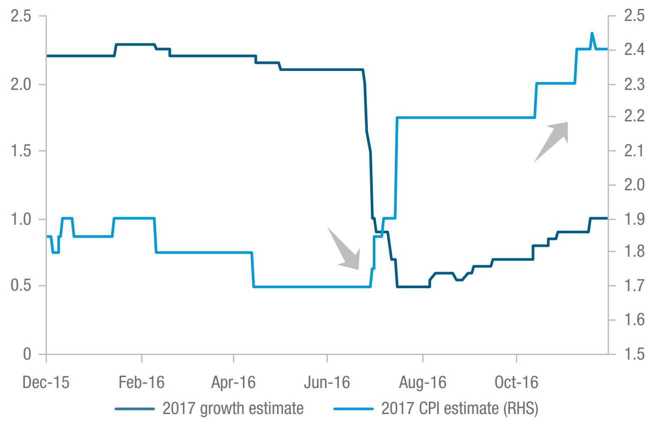
The UK economy has been surprisingly resilient since the Brexit vote, with business confidence bouncing back after an initial slump. However, 2017 is likely to be more challenging as uncertainty around the Brexit negotiations eventually curbs business investment and a weaker GBP boosts inflation, hurting real incomes and consumption. The government has cut its 2017 growth forecast to 1.4% from pre-Brexit estimates of 2.1%, although that remains much higher than consensus estimates which see 0.9% growth next year, the weakest since the 2009 financial crisis.

One of the main casualties of the Brexit vote is the government's fiscal austerity plan. In its first half-yearly budget statement after Brexit, the government abandoned plans to eliminate the budget deficit by 2021, and instead forecasts GBP122 billion of additional deficits over the next five years, half of it due to increased Brexit-related costs. The government will proceed with planned cuts in corporate taxes to 17%, making it the lowest among G20 economies. It also raised income thresholds for tax deductions and announced plans to boost spending on housing, transport and broadband networks to boost productivity.

The UK's upcoming negotiations with Euro area policymakers aimed at retaining access to the European Union common market for British goods and services will be closely watched. The impact of the Brexit talks on the job market remains our key focus – jobless claims have started to rise. A pick-up in unemployment, combined with higher inflation (due to rising import costs from a weaker GBP), could hurt consumption, which accounts for almost 70% of the economy. The BoE, which has already cut interest rates to a record low is likely to tolerate an overshoot in inflation above its 2% target. However, it may come under pressure to raise rates if inflation exceeds 3%.

Figure 5: The UK's 2017 growth forecasts have been downgraded since the Brexit vote, while inflation forecasts have risen as a weaker GBP raises import costs

UK consensus GDP and CPI forecasts for 2017, % y/y



Source: Bloomberg, Standard Chartered

Japan: Tailwind from a weaker JPY

1. Japan's economy remains the most sluggish among major Developed Market economies. However, a weakening JPY, if persistent, is likely to help revive exports, providing a moderate lift to growth
2. Government spending remains a key driver of the economy as business investment and consumption remain lacklustre
3. Prime Minister Abe's four-year old policy ('Abenomics') to reflate the economy is increasingly being questioned due to its inability to deliver on reforms, especially in labour markets
4. Meanwhile, US President-elect Trump's decision to abandon Trans-Pacific Partnership talks is negative for Japan's export sector; it could also delay progress in reforms to open up the economy to competition

Japan's economy is estimated to grow less than 1% in 2017, while inflation is estimated to average around 0.5%, highlighting the economy's persistent deflationary challenges. There is a silver lining – the JPY has weakened more than 12% since the BoJ's policy-shift in September from inflation-targeting to pegging the 10-year government bond yield close to 0%. The decision is likely to put further downward pressure on the JPY in a broadly strong-USD environment.

A weaker JPY, in turn, is likely to provide some boost to the export sector and revive inflationary pressures in 2017. However, significant JPY weakness could lift the cost of raw material imports, especially for energy products whose consumption has surged since Japan shut down its nuclear reactors.

We believe the BoJ's anchoring of long-term yields is also likely to clear the way for the government to issue long-term bonds to fund infrastructure, especially those related to the 2020 Olympics. This could provide an additional lift to growth.

Emerging Markets recovering

1. China is likely to maintain a stable growth of around 6.5% in the run-up to its once-in-five-years Communist Party Congress. This should support growth across the region
2. Asia is likely to remain the biggest contributor to global growth, aided by accommodative monetary policies and robust consumption, especially in domestic demand-focused economies such as India and Indonesia
3. In other Emerging Markets, Brazil and Russia are expected to emerge from two years of recession on the back of a recovery in oil and commodity prices. Falling inflation in both economies should allow central banks to cut rates, supporting the growth upturn
4. The biggest source of risk for Emerging Markets is likely to be external, in particular any protectionist or punitive trade measures from the incoming US administration or from a stronger USD

Asia: China provides stability

Asia ex-Japan is likely to remain the biggest contributor to global growth, with consensus estimates forecasting 5.8% expansion in 2017, compared with 5.7% this year. The region's outlook has shifted from 'uncertainty' to 'stability' over the past year as China's fiscal and credit stimulus helped its economy to stabilise. China's stability, in turn, has helped support the rest of Asia and other Emerging Markets, by putting a floor under global trade and by reviving commodity prices from multi-decade lows.

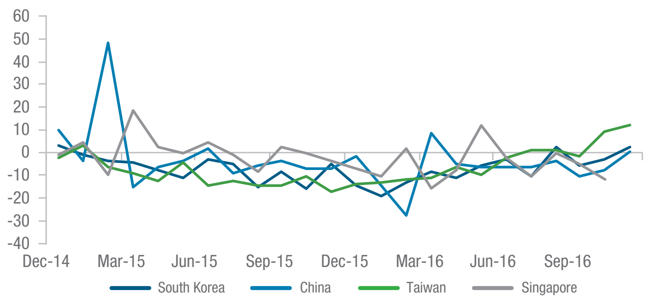
We expect China to maintain its stimulus, as it seeks stability ahead of the Communist Party Congress in Q4 2017 (which will elect the next generation of leaders). Recent measures to control runaway property prices suggest the authorities recognise the risk to financial stability from unbridled property sector expansion and high debt levels. Measures to revamp local government finances and tackle bank bad loans are also positive, as are steps to shift the economy's drivers towards domestic consumption.

One of the biggest risks for Asia is likely to be external. Trump campaigned in the US election to renegotiate trade agreements and impose punitive tariffs on China and other trade partners. Although Trump has been more conciliatory on some issues after the elections, he has reiterated his plans to abandon the Trans-Pacific Partnership trade agreement. Any effort to renegotiate trade pacts is likely to increase uncertainty across Asia, especially in the export-oriented economies including South Korea, Taiwan, Hong Kong, Singapore and Malaysia, which are already struggling with weak exports. Domestic demand-driven economies such as India and Indonesia are less vulnerable to these policy risks.

The USD's recent strength increased capital outflows from the region. The PBoC and other regional central banks are likely to welcome modest currency weakness to support exports which have been contracting for the past couple of years. However, any significant weakness in currencies and higher global rates could undermine financial stability, given the significant rise in the region's debt burden over the past decade. Hence, the recent tightening of capital controls by China to stem a rise in outflows.

Figure 6: Asian exports have been under pressure for the past two years, but there are nascent signs of an upturn

Export growth trend for major Asian exporters, % y/y



Source: Bloomberg, Standard Chartered

Figure 7: Emerging Market growth outperformance over Developed Markets is likely to widen for the first time since the Global Financial Crisis

Emerging Market and Developed Market growth trend and consensus estimate for 2017 (%); Growth differential between EM and DM (%)

Source: Bloomberg, Standard Chartered

Other EMs: Russia, Brazil emerge from recession

Some large Emerging Markets outside Asia are likely to provide the biggest upside to global growth in 2017 as they recover from years of a commodity price-driven downturn. The recovery in oil and mineral prices since the start of the year from multi-decade lows is helping revive export revenues across major Emerging Markets. Meanwhile, a recovery in their currencies since the start of the year (the recent declines notwithstanding) is helping dampen inflation pressures, enabling central banks to start cutting rates.

In particular, Russia and Brazil are likely to contribute the most to the expected acceleration in global growth as the two economies emerge from two years of recession. A rebound in Russia's currency has helped reduce inflation from a 13-year high of almost 17% in 2015 to around 6%, while a recovery in Brazil's currency has led to inflation falling from a 12-year high of almost 11% to around 7%. The decline in inflation has allowed Russia's central bank to extend rate cuts; Brazil's central bank started cutting rates in October from a decade-high level for the first time in this cycle. However, benchmark rates in both economies remain well above inflation, leaving scope for further rate cuts.

Politics remains a key risk in Brazil. President Michel Temer has lost six ministers to a political scandal, but still managed to win Senate approval for an austerity package which will limit public spending. However, several other reforms, including those related to pensions and local government debt, remain major challenges.

Turkey, meanwhile, is focused on curbing likely inflationary pressures caused by a weakening currency. The central bank raised rates in November to 8%, which is likely to weigh on growth.

The USD's latest rise, which has mainly been at the expense of non-Asia EMs, is a broader risk to Emerging Markets. Expectations of more Fed rate hikes could drive the USD and global bond yields higher, tightening financial conditions across Emerging Markets. However, we believe Emerging Markets, especially Asia, are likely to absorb higher US rates, provided the Fed hikes are gradual and reflect a strengthening US economy.

President-elect Trump's campaign proposals to renegotiate trade agreements and impose punitive tariffs on US imports remains a key risk, though. Mexico faces the biggest risk from any renegotiation in NAFTA. Trump's tough stance on immigration is also likely to impact Mexico the hardest. Mexico's currency has weakened the most among major Emerging Markets since Trump's election, forcing the central bank to raise rates 5 times over the past year. Thus, policy risk (especially originating from the US) will be a core focus in the coming months.

KEY RISKS

Stagflation. This involves a sharp rise in inflation without any significant upturn in growth due to structural supply-side limitations such as aging demographics and declining productivity. This scenario is particularly relevant for the US, where the Trump administration's plans to boost spending on infrastructure and cut taxes to stimulate growth clashes with an economy which is already in its eighth year of its expansion and faces an increasingly tight labour market. A stagflation scenario could force the Fed to raise rates faster than expected, further hurting growth.

European political uncertainty. The likelihood of anti-establishment parties gaining ground in the upcoming Euro area elections could call into question the stability of the common market and the future of the euro as a common currency. These concerns are already heightened after the UK's Brexit vote and the Italian referendum, dampening the outlook for business investment. (For instance, in the UK, fixed investment is expected to contract 2.1% in 2017, the biggest decline since the financial crisis). Any resulting growth slump or a return to deflation in Europe could add pressure on European lenders, leading to a full-blown banking crisis.

Trade protectionism. Trump's campaign proposals included imposing punitive tariffs on imports from China and Mexico, abandoning the Trans-Pacific Partnership and renegotiating existing trade agreements such as NAFTA. If implemented, these policies could dampen the outlook for global trade which has already experienced years of slowdown. Emerging Markets face the greatest risk from such an outcome.

Sustained USD gains could hurt US exporters, while encouraging further capital outflows from Emerging Markets. This could dampen global growth. We see US dollar gains as self-limiting, as excessive gains lead to a slowdown in the US economy, causing the USD to give up its gains. The self-adjusting mechanism was apparent in 2015 as well as in H1 2016.

An Emerging Market crisis caused by a hard-landing in China remains a risk. This risk seems more remote today compared with a year ago, given the reforms implemented by China in recent years and the government's proven willingness and ability (seen over the past couple of years) to stabilise growth. We expect China to continue supporting growth ahead of the crucial Communist Party Congress in Q4 2017.

INVESTING IN A WORLD OF FALLING LONG TERM ASSET RETURNS

[Arun Kelshiker, CFA | Trang Nguyen]

- We are moving to a world of lower long-term (7-year) investment returns
- Investors should adjust their return expectations to adapt to this new paradigm
- Investing selectively in alternative strategies, leveraged fixed income and Emerging Markets can benefit a diversified allocation

What's happened

The past twenty years have seen an Emerging Markets crisis in 1998, an equity market collapse in 2000 and most recently the global financial crisis in 2008, which warranted extraordinary quantitative easing measures by central banks.

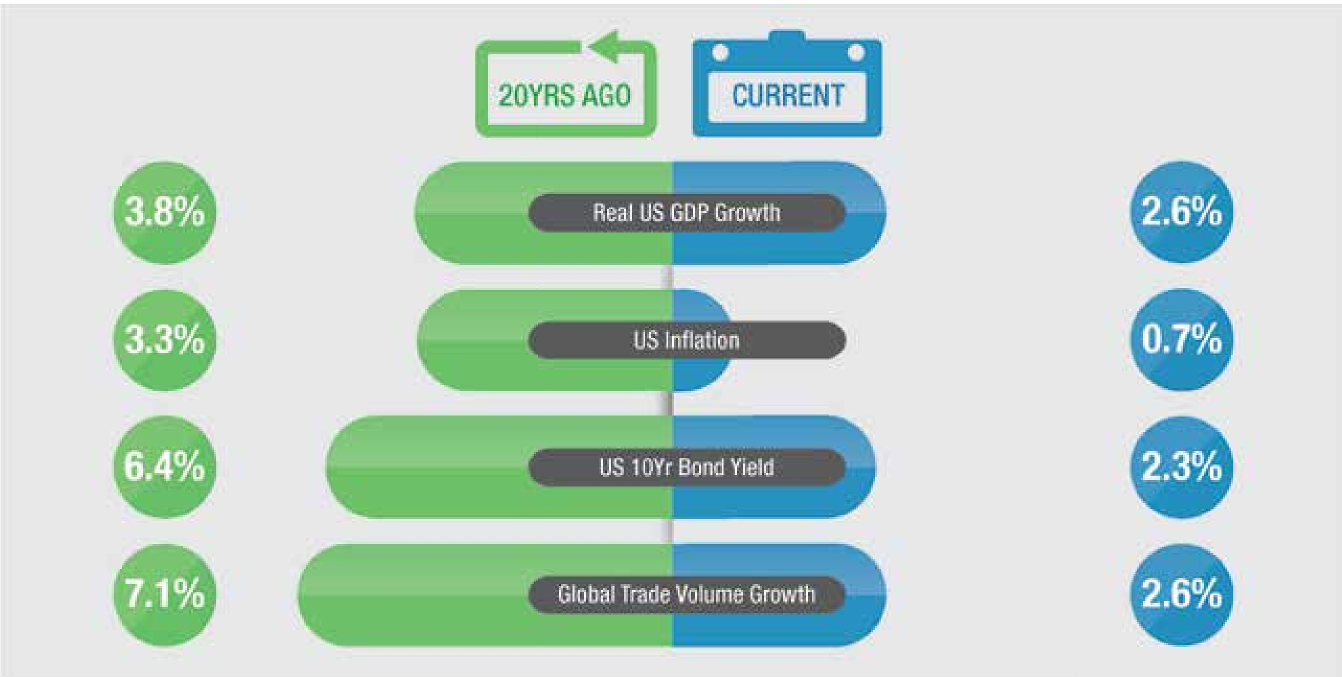
Despite these dramatic events, we have benefitted from a period of equity and fixed income returns in-line with long-term historic averages. Driving these returns has been a healthy combination of secular economic and business trends. The last two decades have seen lower inflationary and interest rate trajectories (Figure 1). Strong global GDP growth was driven by rapid growth in emerging economies including China. We've seen expanding labour-forces and productivity gains which have benefitted from advances in automation and global supply chains. Global trade linkages have increased as new markets have opened up, and corporate profits have seen robust growth.

Today's reality is already questioning previous trends

However, there are signs things may be changing. Inflationary expectations are picking up from an extraordinarily low level, global trade agreements are coming under pressure and both labour productivity and incremental contribution to global growth from China have been slowing. Asset classes have generally become more expensive as valuations have increased across most metrics. The richness of asset valuations has been driven by an ultra-low real interest rate environment. Traditional safe assets provided little to no yield and investors have been forced to look further at riskier assets in search of meaningful returns. Less-supportive secular trends and expensive financial assets suggest future returns are likely to be lower (as shown in Figure 2 on page 21).

Figure 1: Growth over the past twenty years has been driven by strong secular trends

Macroeconomic indicators 20 years ago (end 1996) vs. current (end 2015)



Source: Bloomberg, Standard Chartered

What does this mean for investment allocations?

We can see that the 'efficient frontier' – a combination of traditional equity and fixed income in various proportions – has fallen dramatically (as shown in Figure 3). The implication is allocations might deliver a lower level of return for the same (or even increased) level of risk compared to previous cycles. The lower frontier means investors need to take positions further along the frontier to earn returns closer to previous cycles.

To address this reality, investors have been supplementing investment returns with multi-asset income producing strategies, which have produced favourable multi-year returns.

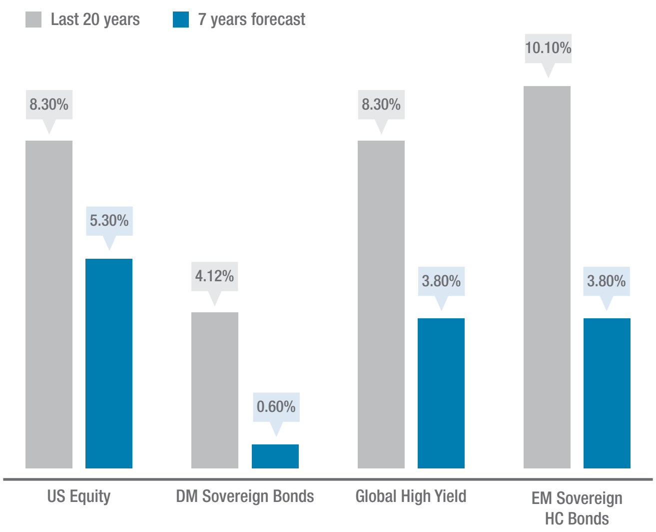
An increasing role for Alternative Strategies

These strategies have played a diversifying role within an asset allocation and have increased in popularity over the past decade due to greater access for investors, improved transparency and more attractive cost structures. Higher risk-adjusted returns can be achieved through many of these strategies, but often with the trade-off being a liquidity premium as capital may only be accessible after a longer timeframe e.g. private equity funds.

Derivative strategies on traditional underlying assets including equities and FX can also provide access to alternative strategies. They allow investors to capture a yield until a structure is triggered, at which point investors receive the underlying asset at a lower price.

Figure 2: Future asset-class returns likely lower than historical averages

Total return (annualised) of different asset classes over the last 20 years[1] vs. 7-year forecast[2]



Source: Bloomberg, Standard Chartered

[1] 20 years taken from Jan 1996 to Nov 2016

[2] Mercer 7 year forward looking asset-class forecasts prepared for Standard Chartered Bank

[3] Combinations of equity and fixed income for various levels of risk

Leveraging fixed income

Given meagre returns on traditional fixed income, investors can also prudently employ leverage to increase their yield and move up the efficient frontier. Leverage comes at a cost, but this can be more than compensated for given coupons of high quality credits and the current cost of borrowing. It is important to note that both interest rates and the costs of borrowing can change and bond defaults can occur.

Emerging Markets can provide structural growth stories

If investors are willing to look beyond short-term market gyrations, Emerging Markets with strong demographic trends can be good areas to invest. These economies are growing at healthy rates, underpinned by improvements in wealth levels coupled with longer term drivers towards domestic driven consumption and industrialisation. One strategy would be to invest selectively into Emerging Markets fixed income; the universe contains many bonds with attractive coupons and high credit quality.

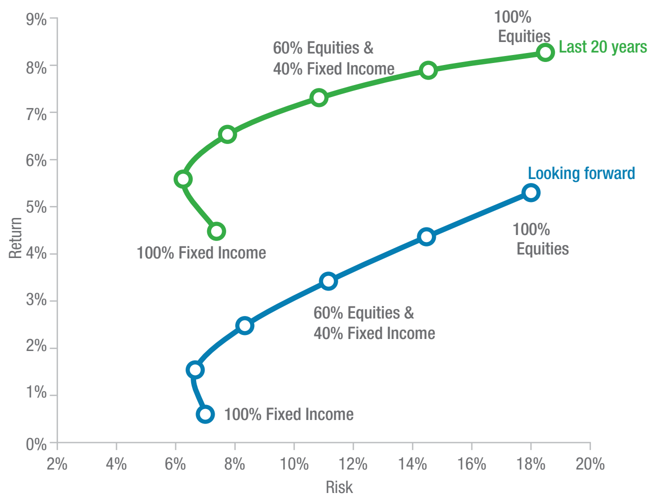
Conclusion

Today's environment of lower returns and greater market fluctuations, although challenging, continues to present opportunities. Investors need to appreciate the changing dynamic of lower returns across asset classes when looking at risk-reward expectations for their investment allocations. This requires an element of behavioural change on the part of an investor to prevent past returns from influencing expectation of future returns (hindsight bias).

Incorporating new strategies and asset class choices can enhance returns and diversify exposure within investment allocations. Investors can benefit from an ever-increasing universe of alternative strategies, which can be valuable allies in the pursuit of investment returns.

Figure 3: 'Collapse of the Efficient Frontier'; investment allocations likely to deliver lower returns at similar levels of risk

Efficient frontiers[3] using 20 years[1] of historical vs. 7-year expected returns[2]



Source: Bloomberg, Standard Chartered

OUR CORE INVESTMENT BELIEFS
HOW WE ARE DIFFERENT

[Alexis Calla | Steve Brice]

5 years ago, when overhauling the existing investment process, our starting point was to design a process that addresses the three key challenges faced by our clients.

First, while clients increasingly have access to information and market views, these are often from a handful of providers. Therefore, the views do not necessarily help investors to form their own opinion on what is appropriate and relevant for them. The selection of pieces we read may also be driven by many of our biases such as confirmation bias.

Second, the views received are generally very global in nature and do not take into account the, to a significant extent valid, home bias of investors.

Third, everybody is susceptible to behavioural biases which can impede our ability to make appropriate decisions.

Therefore, we designed a process that

- seeks and incorporates the views of many different sources of opinions across the major asset classes
- answers our clients key questions, including those related to their local asset classes
- addresses behavioural biases in order to deliver better investment decisions

After extensive research into the challenges of decision-making under uncertainty, we came up with the following core beliefs that led to the process. See page 86 for an outline of our investment process.

"I have no use whatsoever for projections or forecasts. They create an illusion of apparent precision. The more meticulous they are, the more concerned you should be. We never look at projections..."

Warren Buffett

"McKinsey research has found that good (and bad) investment outcomes are mostly attributable not to the analysis that precedes an investment, but to the quality of the process and its adherence to standards of sound and objective decision making."

McKinsey

Diversity trumps expertise in decision-making

Experts are often not the best decision makers within their area of expertise, especially when the domain is characterised by highly uncertain, probability-based outcomes such as investing. This is a hard concept to appreciate, but let's demonstrate with an example.

A strategist has been defending the house view for a month, against the backdrop of conflicting and supporting evidence. The next day she finds herself in the investment committee and is asked to attach a probability to a scenario she has been playing down all month. How easy is it for her to dispassionately do this?

It is not just diversity of people that matter, but also diversity of information and thought process. Accessing a handful of pools of information does not ensure diversity, especially when a consensus is forming. That is not to say the consensus is necessarily wrong, but we believe understanding why it could be wrong is critical to an investment process.

Scenarios trump point forecasts

Forecasts are enticing as they give the perception of certainty. However, nobody knows exactly how things will evolve. Therefore, we believe it is critical to take a scenario-based approach to investing with changes to investment allocations being tweaks in response to changing probabilities rather than dramatic overhauls.

We always try to seek an 'Outside View', which gives a starting point from which to adjust probabilities. For example, an Outside View could be that since 1967, US equities have generated positive returns in 73% of calendar years. From this starting point, we would then examine information that might reduce or increase the chances of positive returns over the next 12 months.

Decision making process is more important than information

In reality, we do not see this as a trade-off as we have access to a wide array of diverse opinions of the major asset classes. However, we believe trying avoid/manage the behavioural biases that we all have, whether we think we do or not, is absolutely critical to achieving superior outcomes.

Relevance may require a limited home bias

While many investment committees focus on a very US/Western-centric approach to investing, we believe this ignores the needs of investors in the rest of the world. Therefore, we seek to generate views that are relevant to your needs rather than somebody who lives on the other side of the world.

MULTI-ASSET
AT A GLANCE

[Aditya Monappa, CFA | Audrey Goh, CFA | Trang Nguyen]

KEY THEMES

A pivot towards growth is more appropriate for a total-return focused investor. For three years, we have recommended a multi-asset income strategy for both income and total-return investors alike. Discussion has shifted from monetary to fiscal policy and to a growing probability of a reflationary scenario. In light of this shift, a growth tilt might be more appropriate for investors focused on total return.

A gradual rebalancing into growth is the preferred approach. Upcoming months might present better entry opportunities into growth assets as we retrace some of the initial euphoria following the US Presidential election and get more clarity on Trump's policies and the Fed's reaction function – we provide an investment map (Figure 3, page 27) that identifies our preferred growth assets in a reflationary scenario.

Multi-asset income strategy remains valid for an income investor. Yield available on assets in our income strategy remains comparable to levels seen at the end of 2015 giving us confidence in the ability to achieve the target yield level. Managing the risk of large declines is a key driver of our approach. As a result, we maintain our conservative stance within the income allocation.

Look to reduce rate-sensitive assets in the income allocation. We expect a pullback in yields as technical indicators suggest the sell-off might be overdone. We look for opportunities to reduce exposure to Emerging Market (EM) USD sovereigns and Developed Market (DM) corporates.

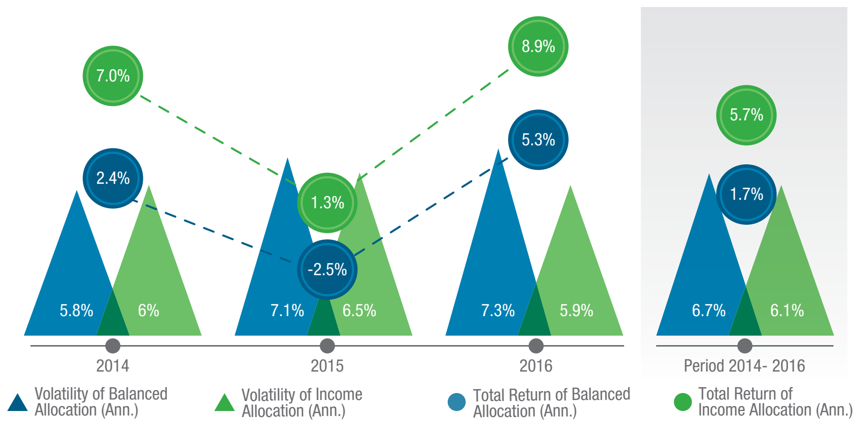
KEY DRIVERS

Income Asset Classes	Weight	Yield	Income Potential	Capital Growth	Risk of Pullback	Comments
Fixed Income	58%	4.8	● (yellow)	● (yellow)	● (yellow)	Portfolio anchor; source of yield; sharp move in yields a risk
Equity Income	25%	4.6	● (yellow)	● (yellow)	● (red)	Key source of income and modest upside from capital growth, potential for large pullbacks
Non-core Income	17%	4.7	● (yellow)	● (yellow)	● (yellow)	Useful diversifier for income and growth

Source: Bloomberg, Standard Chartered. Non-core income includes Preferred Equity, Global REITs, Convertible Bonds and Covered Calls.
Legend: ● Attractive potential/low risk | ● Moderate potential/medium risk | ● Unattractive potential/high risk

KEY CHART

Figure 1: Performance comparison of a balanced and income allocation between 2014 and 2016



Source: Bloomberg, Standard Chartered. For indices used, refer to end note at the conclusion of this section.
*Balanced allocation is a mix of 50% Global Equity & 50% Global Fixed Income.

ADDING A SLICE OF GROWTH

Total return investors should make room for growth

Multi-asset investors are usually faced with a choice related to the mix of income and growth assets within their allocation. In most cases, this choice is primarily driven by investment preference. Those with a cash flow stream to service (for lifestyle or liability reasons) might choose an income tilted allocation while others looking primarily at appreciation of their investments might look at a growth-tilted allocation. In the past few years, this distinction has been driven less by investor preference and more by central bank policy (see Figure 2 on page 26).

Monetary policy stimulus had rendered it almost impossible to generate a sustainable yield from a traditional fixed income allocation. As a result, a multi-asset income strategy, which combined income generating assets across equity, fixed income and non-core income, became the vehicle of choice for the income investor. 2016 was the third year we published a multi-asset income strategy as part of our Outlook publication. A consistent message across these publications was our suggestion that an income strategy was appropriate for both an income investor and a total-return focused investor. This stance has been validated – a comparison of performance of income versus a traditional balanced allocation from 2014 to 2016 (Figure 1 on page 24) shows the yield-focused strategy outperformed the traditional strategy in both absolute terms as well as on a risk-adjusted basis.

Looking ahead, an increasing probability of a reflationary environment suggests a total-return focused investor might now be better served adding growth exposure to their allocation. With a greater focus on fiscal policy, we suggest total-return investors gradually rebalance a portion of their allocation from multi-asset income into growth assets (Figure 2). The use of the word "gradual" is intentional – markets have moved significantly following the US election and we are yet to get complete clarity on President-elect Trump's policies. The upcoming months might present better entry opportunities into our preferred growth assets as we retrace some of the initial euphoria following the election and get a better read on the central bank's reaction function to the new environment.

Figure 2: Trends in multi-asset investing (2009 – today)

Source: Standard Chartered

Our investment map in Figure 3 provides some concrete areas a total-return investor can look to access the beneficiaries of a reflationary environment. Recognising a scenario approach to investing is increasingly important as we move further along in the cycle, we also provide investment opportunities linked to multiple economic scenarios.

Figure 3: A map of potential investment opportunities by economic scenario

DEFLATIONARY DOWNSIDE

Probability
10%

Equity
UK
US
Style – Defensive
Sector – Healthcare

Fixed Income
G3 Long Duration Sov
DM Credit
EM (USD/LC)

Alternatives
Global Macro

Commodities
Energy

MUDDLE-THROUGH

Probability
30%

Multi-Asset Income

Equity
Style – Low Vol, Value, Small Cap
Dividend Equity
Sector – Technology

Fixed Income
DM Credit
EM (USD/LC)

Non-core Income
Preferred Equity
Covered Calls
REITs

Alternatives
Relative Value
Event Driven

Commodities
Energy

REFLATIONARY UPSIDE

Probability
35%

Equity
Style – High Beta
US
Japan
Asia ex-Japan & Non-Asia EM
Sector – Financials, Technology, Small Cap

Fixed Income
TIPS
DM HY
Leveraged Loans
Convertible Bonds

Alternatives
Equity Long Short
Event Driven

Commodities
Base Metals
Energy

INFLATIONARY DOWNSIDE

Probability
20%

Equity
Non-Asia EM
Sector – Materials

Fixed Income
TIPS
Leveraged Loans

Non-core Income
Covered Calls

Alternatives
Global Macro

Commodities
Hard Assets
Precious Metals
Real Estate (Direct)

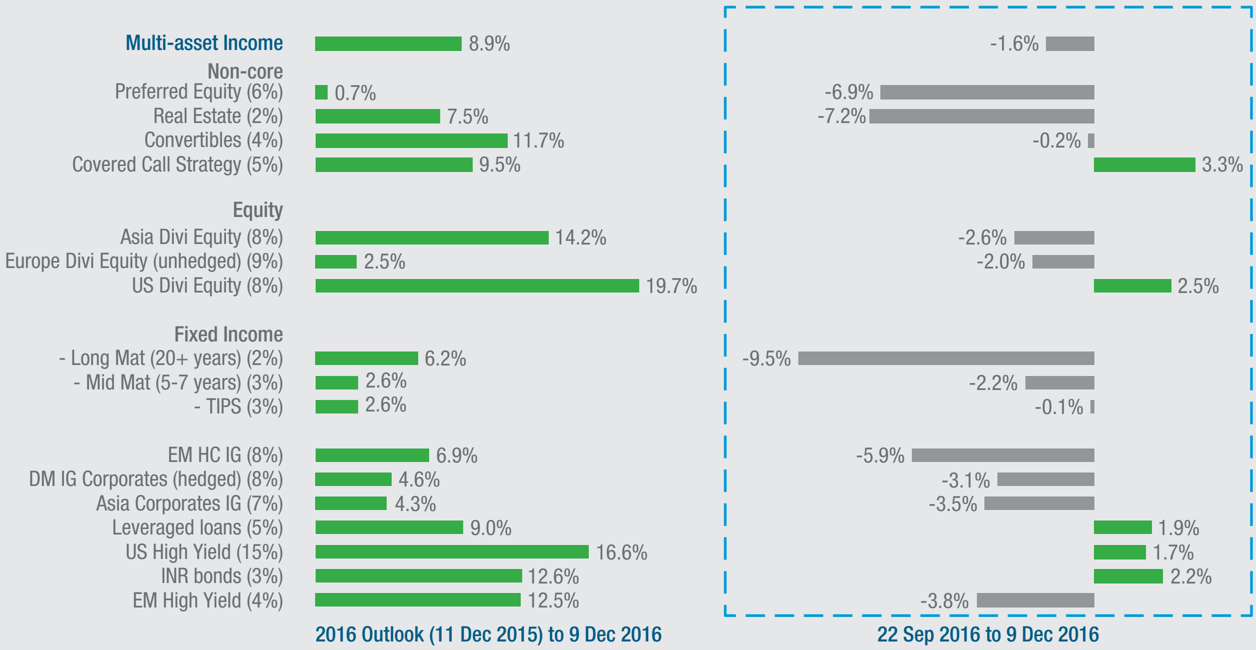
Source: Standard Chartered

Review of multi-asset income allocation in 2016

Looking through a one-year lens, our 2016 multi-asset income allocation has returned 8.9% since we published our Outlook in December 2015. Key contributors to this return have been US assets led by dividend equity, High Yield bonds, convertible bonds and the covered call strategy. EM assets have had a strong run both in fixed income and dividend equity. However, this has been tempered in recent times following the US Presidential election.

Despite delivering positive performance over the year, the trend has started to shift for our income allocation in recent times. Over the past three months (22 September – 9 December 2016), it has returned -1.6%. It is worth looking deeper into recent trends, as this might help with positioning going forward. Three factors contributed to recent performance:

Figure 4: Performance of multi-asset income allocation



Source: Bloomberg, Standard Chartered. For indices used, refer to end note at the conclusion of this section.

1 A sharp move in US government bond yields (85bps between 22 September and 9 December 2016) – this move affected the following rate-sensitive assets within the income allocation: sovereign bonds (Developed and Emerging Markets), Investment Grade Corporate bonds (Developed Markets and Asia), REITs and Preferred Equity.

2 General scepticism towards EM assets – following the US Presidential election, a period of US dollar strength and uncertainty about the trade policy outlook has impacted EM assets. Specifically, in the income allocation, EM hard currency sovereign bonds and Asian dividend equity have seen negative performance over the period. INR bonds have been the outlier delivering positive performance over the period, following yield compression in light of the government's demonetisation initiative.

3 Greater focus on growth and reflation – with the US President-elect being seen as pro-domestic growth in his policy outlook, growth and inflation-sensitive assets have done well in recent times. Beneficiaries in the income allocation have included US dividend equity, convertible bonds (by virtue of their embedded equity optionality) and US High Yield bonds.

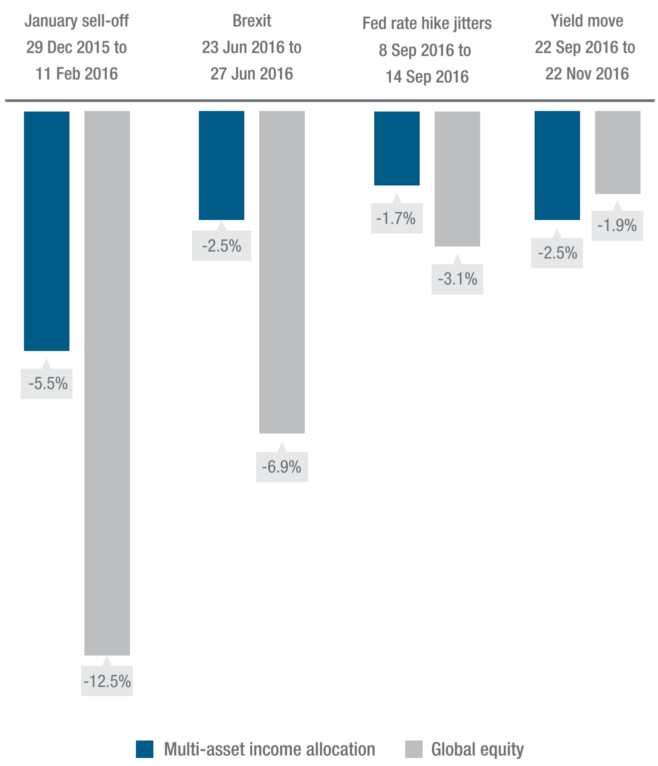
Minor adjustments aside, multi-asset income remains valid for an income investor

Two basic assumptions that have supported the income theme include an accommodative monetary policy environment and low yields in traditional fixed income. Both these assumptions can be reasonably challenged. As discussed in our macroeconomic scenarios, the discussion is shifting from monetary to fiscal policy. Additionally, we've seen a shift towards higher government bond yields in the US on the back of improving macroeconomic data.

Against this backdrop, one might raise the question whether the multi-asset income strategy makes sense? For an investor focused on generating sustainable cash flow, we continue to believe a multi-asset income approach remains valid. A large proportion of global government bonds, the traditional mainstay of an income allocation, provide low to negative yields. This lack of yield from traditional fixed income continues to support a multi-asset income approach with yields available on most assets remaining comparable to levels seen at the end of 2015. This gives us confidence in the ability to achieve the target yield level (4-5%) in 2017. We remain consistent in our usage of the traffic-light framework (see Figure 10 on page 33) to evaluate income assets along three lines – income potential, capital appreciation potential and risk of pullback. We enhance our yield spectrum to provide a regional breakdown of income potential. In addition to a re-evaluation of existing assets, we look at new asset classes through the same lens.

Figure 5: Income strategy had limited declines during equity pullbacks

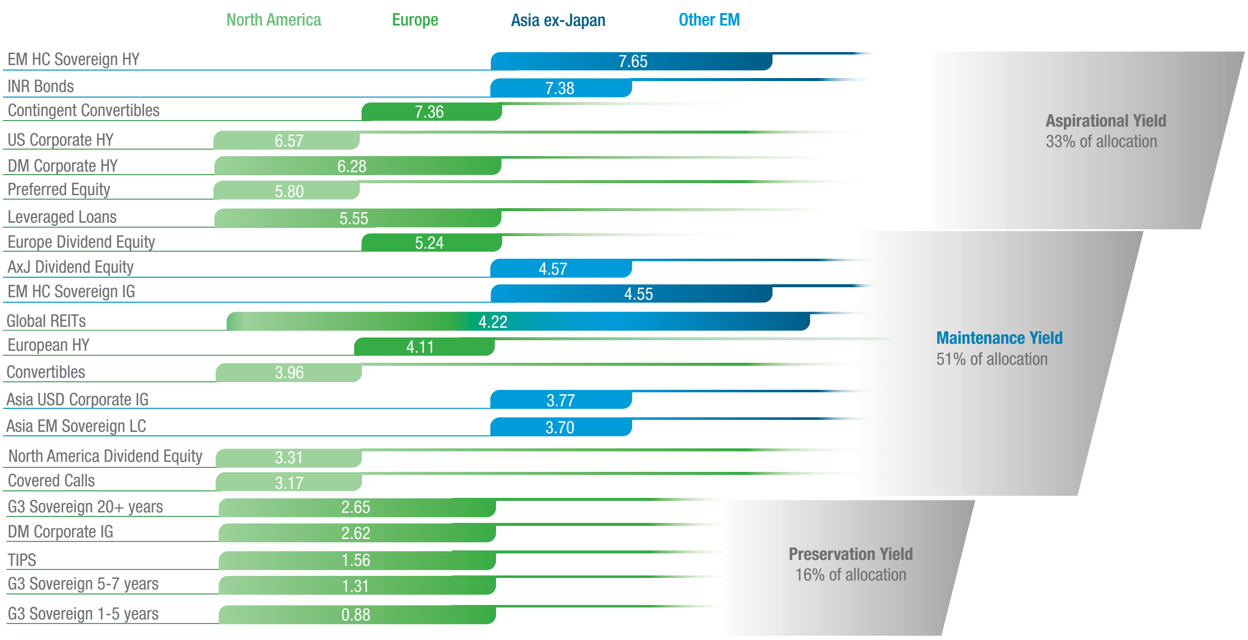
Total return of multi-asset income allocation vs. Global equity



Source: Bloomberg, Standard Chartered
For indices used, refer to end note at the conclusion of this section.

Figure 6: Yield spectrum of income assets broken down by region

Yield to maturity/dividend yield (%) as at 30 Nov 2016



Source: Bloomberg, Standard Chartered. For indices used, refer to end note at the conclusion of this section.

58%

Core Fixed Income

Core fixed income remains the largest portion of our income allocation. We increased our allocation to this asset class at the end of last year (December 2015). Our objective was to adopt a more conservative tilt and manage the risk of large declines within the strategy. The change has worked well in 2016, with the largest decline in the overall allocation being 5.5% since the beginning of 2016 (see Figure 5 on page 29).

Look to reduce interest rate sensitivity within core fixed income

We are comfortable with the overall level of core fixed income – this is consistent with our conservative risk stance within multi-asset income. Within fixed income, we avoid making any changes at the present moment. As highlighted earlier in this publication, we expect a pullback in yields with technical indicators suggesting the sell-off might be overdone. The table of interest-rate sensitivity in Figure 7 is our guide to relative opportunities that exist in the event of a move in yields. We are watching the following areas for potential rebalancing opportunities:

- Look to reduce our EM USD sovereign bond exposure. Specifically, the Investment Grade component offers around 4% yield, high sensitivity to USD interest rates and would suffer in an environment of EM scepticism. The proceeds from this rebalancing would be moved to leveraged loans which offer a higher yield, low sensitivity to interest rates and positive dynamics from an improving US growth environment.
- Look to reduce our allocation to DM Investment Grade corporate bonds. The proceeds from the rebalancing would be used to moderately increase our allocation to TIPS which offer better risk-reward prospects in an environment of rising inflation expectations.

Figure 7: Total return of fixed income assets assuming different changes in yield

Yield to maturity, duration* for fixed income assets as at 30 Nov 2016

	EM HC Sovereign High Yield	INR Bonds	US Corporate High Yield	Leveraged Loans	EM HC Sovereign Investment Grade	Asia USD Corporate Investment Grade	G3 Sovereign 20+Yrs	DM Corporate Investment Grade	TIPS	G3 Sovereign 5-7Yrs
Yield to Maturity	7.65%	7.38%	6.57%	5.55%	4.55%	3.77%	2.65%	2.62%	1.56%	1.31%
Duration*	5.61	5.31	4.20	0.25	7.36	5.30	18.04	6.62	1.58	5.55
Change in yield										
-1.50%	16.1%	15.3%	12.9%	5.9%	15.6%	11.7%	29.7%	12.6%	3.9%	9.6%
-1.00%	13.3%	12.7%	10.8%	5.8%	11.9%	9.1%	20.7%	9.2%	3.1%	6.9%
-0.50%	10.5%	10.0%	8.7%	5.7%	8.2%	6.4%	11.7%	5.9%	2.4%	4.1%
0.00%	7.7%	7.4%	6.6%	5.6%	4.6%	3.8%	2.7%	2.6%	1.6%	1.3%
0.50%	4.8%	4.7%	4.5%	5.4%	0.9%	1.1%	-6.4%	-0.7%	0.8%	-1.5%
1.00%	2.0%	2.1%	2.4%	5.3%	-2.8%	-1.5%	-15.4%	-4.0%	0.0%	-4.2%
1.50%	-0.8%	-0.6%	0.3%	5.2%	-6.5%	-4.2%	-24.4%	-7.3%	-0.8%	-7.0%

Source: Bloomberg, Standard Chartered. For indices used, refer to end note at the conclusion of this section.
*Duration is a measure of the sensitivity of price of a fixed income investment to a change in interest rates. Duration is measured in years.

25%

Core Equity

Dividend equity continues to act as a vital component of multi-asset income. The asset class offers attractive yields in the 3-5.5% range and potential for capital appreciation in a few sectors. While large pullbacks remain a challenge within dividend equity, strong risk management (favouring regional and sector diversification instead of chasing the highest yields) should mitigate this risk. Consistent with our traffic light framework, we decide to reduce our allocation to US dividend equity given the limited yield on offer, high relative valuations and significant sensitivity to rising interest rates. We increase our allocation to Europe dividend equity, while maintaining our allocation to Asia ex-Japan.

Reducing our allocation to US dividend equity

We pare our allocation within US dividend equity – yields are low relative to other regions and the valuation is on par with US traditional equity at 16.5x 12 month forward price-earnings ratio. It's defensive properties and limited exposure to the financial sector suggests it may benefit less from a rise in interest rates relative to traditional US equity. However, given this asset class tends to see lower pullbacks relative to dividend equity in other regions, a small allocation is still warranted.

Policy divergence supportive of European dividend equity near term

An accommodative policy environment should sustain the 'search for yield' in Europe. More than 70% of European dividend equities offer a higher yield compared to their respective corporate bonds. Additionally, this asset class receives further support from the divergence in global interest rate policies. The US is expected to hike twice in 2017 while the European Central Bank should remain highly accommodative relative to the US, sustaining the search for yield within Europe. Additionally, given our view on potential weakness in EUR and GBP (UK dividend equities are almost 50% of the index), we believe it is prudent to hedge currency exposure within Europe dividend equities at the present time.

We believe European dividend equities can offer a good reflationary hedge against rising yields in the US. Financials (bulk of which are insurance companies), the largest sector, has one of the highest positive correlations to US 10-year Treasury yield. The sector offers an attractive yield of 5.6% and a low 1x price-to-book valuation. While the potential for pullbacks is significant, an improving outlook for growth and capital solvency among insurers in Europe should contribute to better dividend growth – a key overhang on the sector's performance in recent years.

Figure 8: A three-pronged approach to assessing Equity Income

Income Potential, Capital Growth and Risk of Pullback

Asset Classes	Yield	Income Potential	Capital Growth	Risk of Pullback	Comments
North America	3.3	🔴	🟡	🟡	Fair to slightly rich valuations; subdued sales/profit growth mean below average returns; some sectors attractive
Europe	5.2	🟢	🟢	🟡	Fair valuation; ECB support; attractive yield; challenges from global growth; FX and a busy election calendar in 2017 are wild cards
Asia ex-Japan	4.6	🟢	🟡	🔴	Good payouts; selectively attractive valuations, but pullback a risk from challenges in China/US growth, earnings, Fed and leverage

Source: Bloomberg, Standard Chartered

Legend: 🟢 Attractive potential/low risk | 🟡 Moderate potential/medium risk | 🔴 Unattractive potential/high risk

We believe European dividend equities can offer a good reflationary hedge against rising yields in the US.

Standing firm on Asian dividend equity
On Asia dividend equities, we choose to maintain our allocation. This asset class retraced a significant portion of its year-to-date gains post the trough in the US 10-year Treasury yield on 22 September 2016 – not a surprise, given the region tends to experience greater risk of a pullback on concerns over higher US interest rates and weaker Asian currencies.

Financials account for the bulk of dividend income within Asia with Banks, particularly in China and Singapore, as key contributors. This sector has been resilient recently, on the back of its domestic focus, high dividend yield and cheap valuations. We are generally sanguine on Asia dividend financials.

The technology and telecommunication sectors are the second and third largest sectors within Asia respectively. Both sectors deliver attractive yields in excess of 5%. Bolstering the yield is an improving consumption story in the US which should support demand for technology products. Of course, the evolving US trade policy outlook and rising yields remains a risk to these sectors.

Figure 9: Europe Dividend equities have recently followed US bond yields closely – but a gap has opened up for now

MSCI Europe dividend Equity relative to MSCI World vs. US Treasury 10-year yield

Source: MSCI, Bloomberg, Standard Chartered
For indices used, refer to end note at the conclusion of this section.

17%

Non-core Income

Maintain lower exposure to interest rate sensitive assets in non-core income
The benefit of non-core income is primarily the diversification it brings to the allocation through a lower correlation with equity and fixed income (while offering a reasonable yield). For convertible bonds and covered calls, the benefits continue to make sense. Convertible bonds offer equity market optionality (which should be a positive in a reflationary scenario), but with a downside buffer. Additionally, our convertible bond benchmark contains a large allocation to the technology sector which could benefit from tax schemes offered by the new US administration. Covered call strategies should provide income while helping to buffer some of the volatility. They are potentially most effective for markets or sectors where we expect positive, but range-bound returns.

On real estate, we choose not to increase our allocation given middle-of-the-road yields, a large potential for pullbacks and a high sensitivity to rising interest rates. This was evident in 2016 where we saw large swings in performance as the tone on Fed policy went from dovish early in the year to hawkish later on.

Our Preferred Equity exposure has been an outstanding performer for the past few years. While a subset of this asset class has a stated maturity date (and hence is less susceptible to rising rates), the bulk of the exposure is in perpetual preferreds (no stated maturity date), which carry the greatest interest rate risk. With this in mind, we reduce our allocation to US Preferreds in favour of Contingent Convertibles (CoCos). We believe CoCos are attractive due to the high yield on offer, relatively low sensitivity to rising yields and improving bank credit quality over the past few years. *Please note: The Financial Conduct Authority (FCA) has introduced Permanent Marketing Restrictions on the sale of CoCos to residents of the EEA.*

Figure 10: A three-pronged approach to assessing income assets

Income Potential, Capital Growth and Risk of Pullback

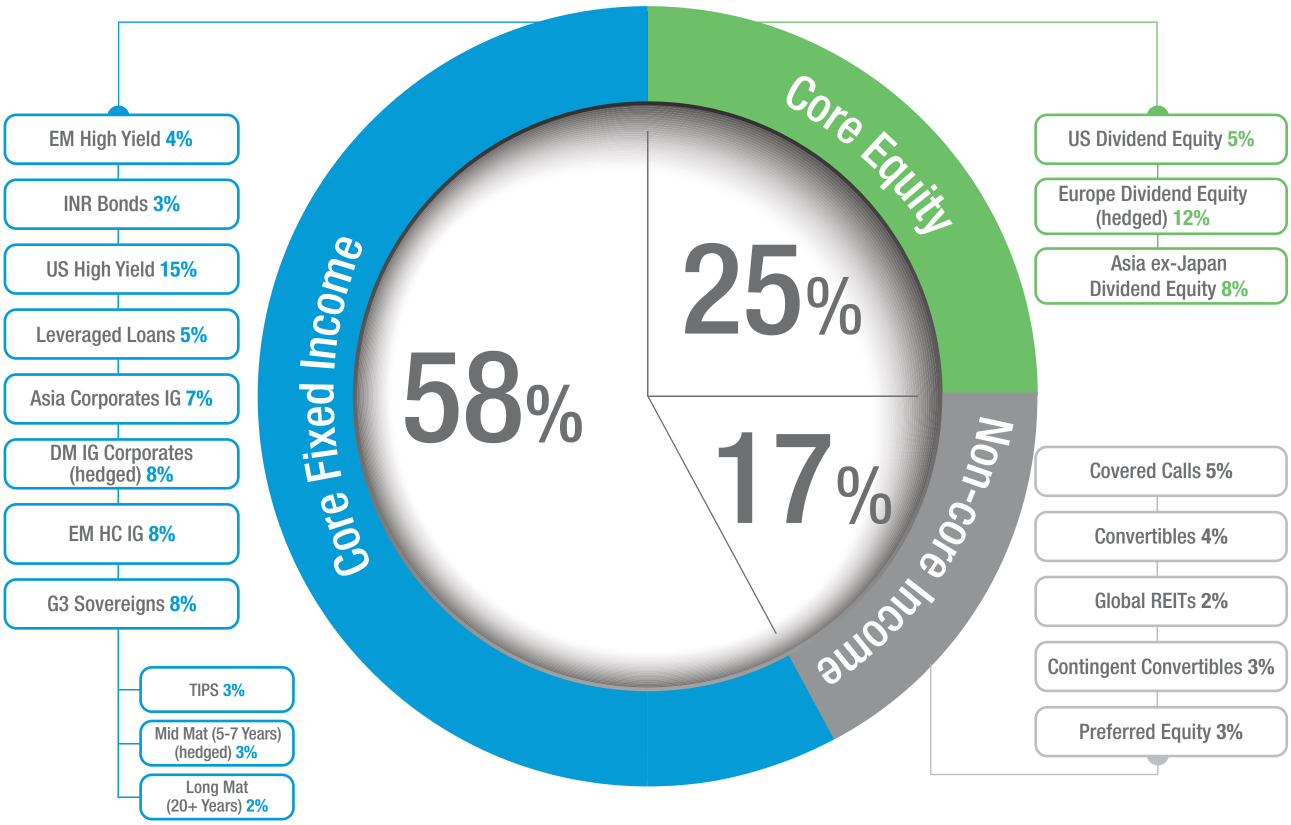
Asset Classes	Yield	Income Potential	Capital Growth	Risk of Pullback	Comments
Fixed Income	4.8	🟡	🟡	🟡	Portfolio anchor; source of yield; some interesting ideas but not without risks
Leveraged Loans	5.6	🟢	🟡	🟡	Attractive alternative to traditional HY exposure; senior in capital structure to simple HY bonds; small yield penalty in return; low sensitivity to changes in US interest rates
Corporate – DM HY	6.3	🟢	🟡	🟡	Attractive yield; high coupons and low interest rate sensitivity; peak in energy and materials sector defaults likely behind us
EM HC Sovereign Debt	5.9	🟢	🟡	🔴	Need to be selective given diverse risk/reward in IG, HY bonds; High sensitivity to rise in US interest rates a risk; commodity exposure may be a support; valuations reasonable
Asia EM Sovereign LC	3.7	🟡	🟡	🔴	Broad risk/reward unattractive; local economic outlook stable, rate cut cycle well advanced; FX, flows the main risks; idiosyncratic stories only
INR bonds	6.9	🟢	🟡	🔴	Structural story playing out; carry play; credible central bank, reforms; foreign demand a recent risk; FX stability needed
Investment Grade	2.7	🔴	🟡	🟡	Portfolio anchor, structural carry; some interesting ideas but interest rate sensitivity a risk
Corporate – DM IG	2.6	🔴	🟡	🟡	Valuations still reasonable; sensitivity to changes in interest rates a risk, but yield premium offers a buffer
Corporate – Asia IG	3.8	🟡	🟡	🟡	Fairly valued, stable quality, China growth stability and strong regional demand are supports; CNY trend direction, China concentration are risks
TIPS	1.6	🔴	🟢	🟢	Offers value as an alternative to sovereign bonds; impact of rate rise similar to G3 sovereign but offers exposure to an eventual jump in US inflation
Sovereign	1.4	🔴	🔴	🟡	Little value in reflationary scenario; US fiscal stimulus, Fed messaging a risk; beneficial in deflation risk scenario; prefer higher yielding/high quality markets (US Treasury, AU, NZ)
Equity Income	4.6	🟡	🟡	🔴	Key source of income and modest upside from capital growth
North America	3.3	🔴	🟡	🟡	Fair to slightly rich valuations; subdued sales/profit growth mean below average returns; some sectors attractive
Europe	5.2	🟢	🟢	🟡	Fair valuation; ECB support; attractive yield; challenges from global growth; FX and a busy election calendar in 2017 are wild cards
Asia ex-Japan	4.6	🟢	🟡	🔴	Good payouts; selectively attractive valuations, but pullback a risk from challenges in China/US growth, earnings, Fed and leverage
Non-core Income	4.7	🟡	🟡	🟡	Useful diversifier for income and growth
Preferred	5.8	🟢	🟡	🔴	Attractive yield and exposure to financials; risk from higher rates may not be completely offset by improvement in bank's underlying credit
CoCos	7.4	🟢	🟡	🔴	Attractive due to the high yield on offer, relatively low sensitivity to rising yields and improving bank credit quality over the past few years
Convertibles	4.0	🟡	🟡	🟡	Moderate economic expansion and gradual pace of rate hikes should be good for convertibles. Risk: US rate policy mistake
Global REITs	4.2	🟡	🟡	🔴	Yield diversifier; stable real estate market; risk from higher rates, valuations stretched in some regions. Potential for large pullback
Covered Calls	3.2	🔴	🟡	🟡	Useful income enhancer assuming limited equity upside

Source: Bloomberg, Standard Chartered

For indices used, refer to end note at the conclusion of this section.

Legend: 🟢 Attractive potential/low risk | 🟡 Moderate potential/medium risk | 🔴 Unattractive potential/high risk

Figure 11: Revised multi-asset income allocation for 2017



Source: Bloomberg, Standard Chartered
For indices used, refer to end note at the conclusion on this section.

Conclusion

For the first time since 2014, we suggest a different approach for a total-return investor as compared to an income investor. Over the past three years, the multi-asset income allocation has been a theme we have highlighted to *both* income and total-return focused investors. Our conviction in the theme has been validated by its three-year performance – it has delivered a higher risk-adjusted total return versus a balanced allocation over this period.

Towards the end of 2016, we've seen some of the fundamental conditions supporting the multi-asset income theme begin to dissipate. Monetary policy is being tempered or potentially reaching the limits of its effectiveness. Government bond yields have moved in an upward trajectory particularly in the United States. While it's important to avoid a knee-jerk reaction to short-term indicators, an accumulation of factors point to a broader shift in the macroeconomic landscape. Against this backdrop, we advise total-return investors to gradually rebalance a portion of their multi-asset income allocation into growth assets. To help this process, we provide a useful investment map highlighting our preferred growth assets that should benefit in a reflationary scenario.

For income investors looking to generate a sustainable 4-5% yield, a multi-asset income approach remains valid as we enter 2017. Yield available on most assets in our income allocation remains comparable to levels seen at the end of 2015 giving us confidence in the ability to achieve the target yield level. With managing risk of large pullbacks being a key driver of our strategy, we maintain a conservative stance within the income allocation. We've seen an increase in pullbacks of interest-rate sensitive assets. In light of this, we look for opportunities to reposition the income allocation in areas that might benefit from an increase in interest rates and reduce exposure to rate-sensitive assets. We believe this rebalancing should allow yield-seeking investors to receive a steady stream of cash flows in 2017.

End note:
Indices are CRISIL Composite Bond Fund Dollar, Barclays US Corporate High Yield TR, J.P. Morgan EMBI Global Diversified High Yield, Barclays Global High Yield TR, JACI Non-Investment Grade TR, S&P Leveraged Loan TR, MSCI AC Europe High Dividend Yield, SPDR Wells Fargo Preferred Stock ETF, MSCI EM Asia High Dividend Yield, J.P. Morgan EMBI Global Diversified Investment Grade, Barclays Pan-European High Yield, FTSE EPRA/NAREIT Asia REITs TR, Chicago Board Options Exchange S&P 500 BuyWrite, FTSE EPRA/NAREIT Developed North America REITs TR, S&P China Corporate Bond, JACI Investment Grade TR, FTSE EPRA/NAREIT Europe REITs TR, MSCI North America High Dividend Yield, Citi Non-MBS WorldBIG 20+ Yr, Citi WorldBIG Corporate, BC US Conv 500MM Face Liquidity Constraint TR, Citi Non-MBS WorldBIG 5-7 Yr, Citi Non-MBS WorldBIG 1-5 Yr, Barclays US Treasury TIPS 0-5 Yr TR, MSCI EMU High Dividend Yield Net Local, MSCI ACWI High Dividend Yield Net TR, MSCI Daily TR Net USA, MSCI Daily Net TR Europe Euro, MSCI AC Daily TR Net Asia Ex Japan, MSCI AC World Daily TR Net, Barclays Global Contingent Capital TR Index Value Unhedged USD

DERIVATIVES

Higher rates = more opportunities for selling options

Easy monetary policy and ultra low rates is a key reason why volatility has been low over the last few years. Such an environment forced investors to search for yield, and many did so via selling options, suppressing volatility in the process.

In the event of a reflationary scenario, which is likely to push yield levels higher and lead to further rate hikes, downward pressure on volatility should gradually abate. Since the creation of VIX (the US stock market Volatility Index) in 1990, there have been two cycles of US rate hikes. On both occasions, the VIX rose as rates went higher.

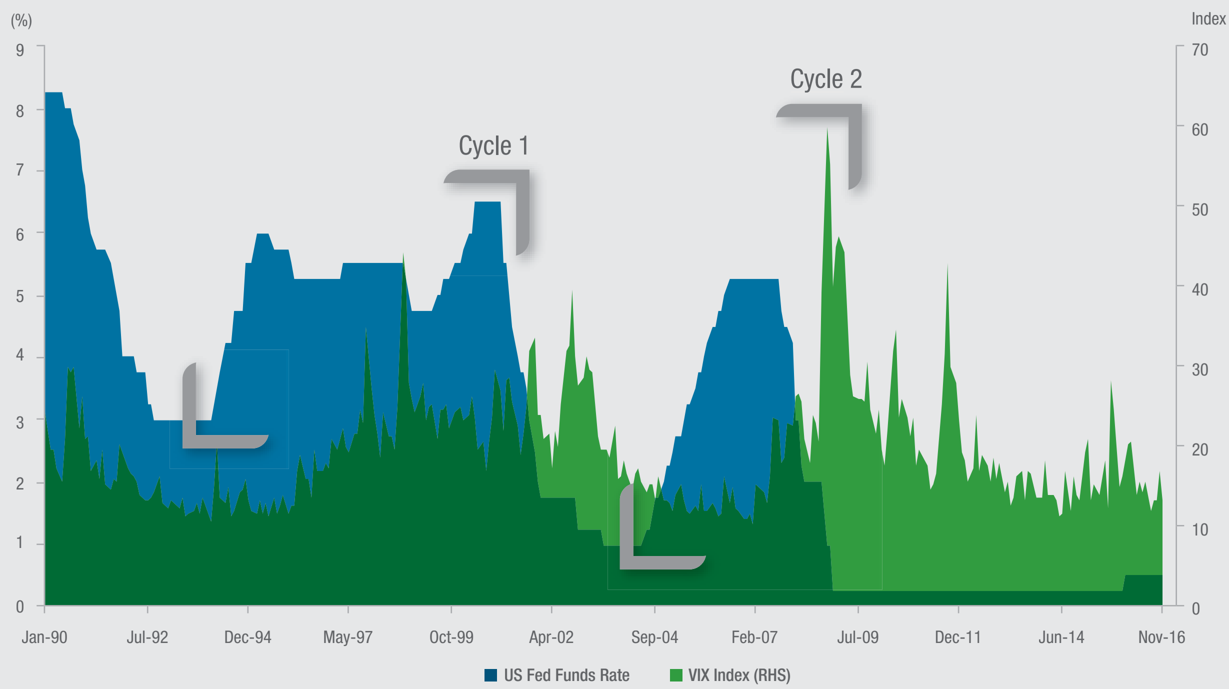
All else being equal, the higher the volatility level, the more yield option sellers receive. In selling put options, investors risk receiving the underlying if it drops below the strike level at option expiry. However, as expressed in the equity section, we have a positive stance towards equities in 2017. Thus, we believe investors will find an equity option-selling strategy to be more attractive in the year 2017 versus 2016. In order to come up with thematic option ideas for 2017, we compare derivatives markets versus fundamental data, and noticed a couple of areas that could be of interest to option sellers.

First, in the currency space, the ranges of analysts' forecast for AUD/USD and NZD/USD are narrower than implied by the options market. Thus, selling options on AUD/USD and NZD/USD would give breakevens that cover more than 90% of the range of analysts' forecast for these two currencies. Note that we are bullish these two currencies.

Such ideas are tougher to find for equity indices. To a large extent, this is due to the mostly bullish consensus forecast for equities in 2017. Thus, for prudence, we use another approach, and compare 12M forward price-earnings ratio (P/E) of S&P 500, EuroStoxx 50, FTSE 100 and Hang Seng Index, against their respective 10-year average P/E. Selling put options on the Hang Seng Index would allow investors to earn a reasonable yield at the risk of acquiring exposure to Hong Kong equities at historically attractive valuations. As we move through 2017, we would look for similar opportunities in other equity markets.

Figure 12: Volatility levels rose over the last two cycles of US rate hikes

VIX vs. Fed Fund Rates since 1990



Source: Bloomberg, Standard Chartered.

MULTI-ASSET
COMBINING ALTERNATIVE STRATEGIES

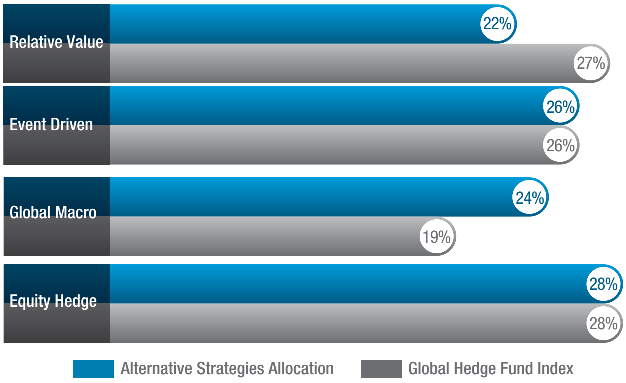
[Arun Kelshiker, CFA | Trang Nguyen]

- Investors have become sceptical of the merits of alternative strategies, given their lacklustre performance this year; we continue to advocate their use in diversified allocations
- Alternative strategies provide unique return profiles. Combining the four broad sub-strategies in an allocation (see Figure 13) provides some all-weather benefits; a good complement to traditional equity and fixed income
- The recent new class of alternatives termed 'liquid strategies' can provide an easier route to access this asset class

Alternative strategies still make sense in an allocation despite lacklustre performance in 2016
While the overall asset class has been a marginally positive performer in 2016, specific alternative sub-strategies, e.g. global macro, have had a poor year as shared in our Alternatives section (see page 69). Insurance-like properties of these strategies did not work as they were generally positioned for deflationary or risk-off scenarios, which did not come to pass. While we recognise 2016 has been a difficult year, we continue to advocate the use of alternative strategies within a diversified allocation.

Figure 13: Favouring Global Macro on a relative basis

Proposed allocation to major alternative strategy groups as compared with the benchmark* allocation



Source: Hedge Fund Research Inc., UBS, Standard Chartered
*HFRX Hedge Fund Index is a common benchmark used to represent all of the main hedge fund strategies. Composition of benchmark proxied by UBS HFRX Global Hedge Fund Index ETF (31 October 2016)

While investors are increasingly considering a global reflationary scenario in 2017 (as discussed in our Macro section), a number of alternate scenarios continue to exist. In this context, we maintain our allocation towards alternative strategies given their insurance-like qualities.

Investors increasingly spoilt for choice within alternative strategies
A private investor has far greater access to a variety of alternative strategies than previously existed. These strategies have been following a trend towards increased transparency and greater liquidity. A key benefit is diversification of traditional equity and fixed income exposure and improving the overall risk-adjusted return. Investing in alternative strategies allows for greater focus on absolute returns. Strategies also generally use leverage, which allows managers to 'magnify' investment returns from asset mispricing.

Liquid alternatives are a relatively recent offspring of traditional alternative strategies. They provide investors with access to the alternative asset class, but on better liquidity terms. This addresses one of the concerns investors have traditionally had in regards to alternative strategies. Qualitatively, often they may have lower amounts of leverage than their traditional counterparts and can be selective with respect to underlying assets given the greater focus on liquidity.

Combining alternative strategies in an allocation provides all-weather benefits
In our 2016 mid-year outlook 'Navigating Headwinds', we talked about how alternative strategies can complement a traditional allocation. We now explore how private investors can maximise the benefit of these strategies by discussing how to "combine them together within a standalone allocation". An allocation of alternative strategies can provide an excellent 'all weather' approach to preserving capital.

Figure 14: Alternative strategies sub-groups

	Description	Conditions which may be favourable
Equity Hedge	In essence buying undervalued stocks and selling overvalued stocks; examples include global, regional and specific sector fundamental based equity long-short and equity market neutral strategies	Equity hedge strategies, including equity long-short, generally have greater opportunities to perform well when stocks and sectors have wide performance dispersion within an equities universe
Event-Driven	Taking positions based on an event; examples include merger arbitrage, special situations and credit arbitrage strategies	Event-driven strategies can flourish in environments where companies proactively pursue value enhancing actions including spin-offs and buybacks
Global Macro	Looking to exploit themes, trends and asset class relationships (correlations) at a global level, generally with leverage; examples include discretionary thematic global macro and systematic macro trend following strategies	Trend following strategies perform well in the absence of short and frequent market upward and downward movements; discretionary strategies are highly dependent on the success of specific themes
Relative Value	Looking to take advantage of differences in pricing of related financial instruments; examples include fixed income sovereign, corporate and convertible arbitrage strategies	Sharp sell-offs and sharp rallies in credit can provide improved opportunities for long short credit strategies within the relative value group

Source: Hedge Fund Research Inc., Standard Chartered

Using one of the most popular benchmarks for alternative strategies provided by Hedge Fund Research Inc., we can categorize them into four broad groups as shown above.

Global Macro has low correlations with equity as well as the other three alternative strategies (Figure 15), which highlights its diversification benefits within an overall allocation. Equity Hedge and Event Driven strategies, with higher equity correlations, can act as effective substitutes for traditional equity. Relative Value strategies are positioned in-between Global Macro strategies (diversifying) and Equity Hedge and Event Driven (equity substitutes).

When building our 'best mix of alternative strategies', we keep our key thesis of diversification and maintain a good split between weightings of the broad groupings. As shared in the Alternatives section, Global Macro strategies offer value within an allocation with their insurance-like characteristics. Relative Value is the least favoured of the four groups. Against this backdrop, our allocation would draw its base weights from the benchmark and make an adjustment to tilt in favour of Global Macro strategies over Relative Value. Weights for the other two categories would be in line with the benchmark as shown in Figure 13 on page 36.

A review of our proposed allocation using historical data demonstrates its benefits. Since 2000, the Alternative Strategies Allocation has generated an annual return of 3.1%, on par with global equity, but with only 21% downside capture (on average, the Alternative Strategies Allocation would only have 21% of the decline of global equity) as shown in figures 16 and 17 on page 38. While traditional fixed income might look equally attractive from a return and decline perspective, it's important to remember the fall in bond yields (approx. 400bps) we've seen over this period. Against this backdrop, the return prospects for traditional fixed income going forward are relatively muted. The negative correlation of alternative strategies to fixed income should be looked at favourably in this context.

Figure 15: Global Macro shows good diversifying benefits within an overall allocation

Long term correlation between traditional asset classes and alternative strategies (31 Dec 1999 till 30 Nov 2016)

	Equity	Fixed Income	Equity Hedge	Global Macro	Event Driven	Relative Value
Equity	1.00					
Fixed Income	0.02	1.00				
Equity Hedge	0.85	-0.18	1.00			
Global Macro	0.23	-0.11	0.32	1.00		
Event Driven	0.73	-0.18	0.77	0.21	1.00	
Relative Value	0.43	-0.15	0.43	0.12	0.46	1.00

Source: Hedge Fund Research Inc., Bloomberg, Standard Chartered

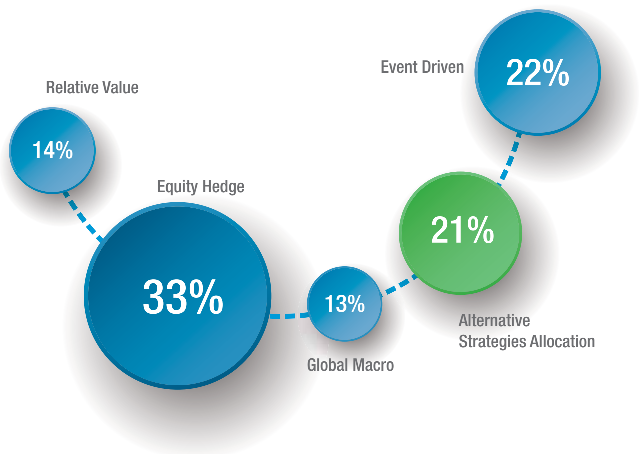
Figure 16: Annualised return of Alternative Strategies Allocation is on par with global equity, but has better capital preservation since 2000

Total return and maximum decline for traditional assets and Alternative Strategies Allocation across different time periods

Source: Hedge Fund Research Inc., Bloomberg, Standard Chartered

Figure 17: The Alternative Strategies Allocation has limited downside capture* compared with global equity

Alternative strategies downside capture vs. global equity (Jan 2000 to Oct 2016)



Source: Hedge Fund Research Inc., Bloomberg, Standard Chartered
*Downside capture is the relative performance of an asset versus an index, during period when that index has dropped. It is expressed in percentage terms.

Conclusion

Alternative strategies provide non-traditional investment avenues for private investors, adding an arsenal of instruments which ultimately can improve long-term risk-reward profile for an investment allocation. Each of these strategies can vary materially suggesting an Alternative Strategies Allocation can significantly enhance value by preserving capital (insurance-like quality) while also allowing good performances during both up and down markets.

KEY INVESTMENT THEMES AT A GLANCE

1 Multi-asset income allocation to deliver positive absolute returns

2 A balanced allocation (mix of 50% Global Equity & 50% Global Fixed Income) to outperform multi-asset income allocation

3 Our alternative strategies allocation to deliver positive absolute returns in 2017

BONDS
AT A GLANCE

[Manpreet Gill | Abhilash Narayan]

KEY THEMES

The rising likelihood of higher inflation leads us to look for opportunities to scale back our bonds exposure and focus on lowering interest rate sensitivity. We expect the 10-year US Treasury yield to rise moderately, closing 2017 between 2.5%-3.0%, assuming the reflationary scenario is confirmed.

We prefer corporate bonds to sovereign bonds. We prefer HY bonds in the US and Europe, but are cautious on HY in Asia. We view US floating rate senior loans as an attractive alternative to US HY bonds.

In the near term, we expect a pullback in yields as technical indicators show the current sell-off may be overdone. We would use such a pullback as an opportunity to lower our exposure to Developed Market (DM) Investment Grade (IG) and Emerging Market USD Government bonds.

Entering 2017, we maintain our view to hold an average maturity profile of about 5 years in USD bond allocations in an effort to cap sensitivity to rising interest rates.

KEY DRIVERS

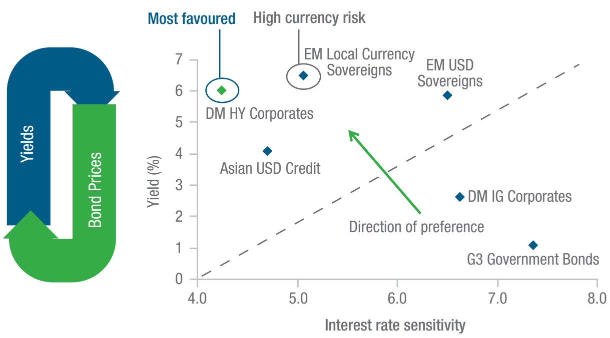
Asset Allocation	View	Rates Policy	Macro Factors	Credit Spreads	Currency	Comments	2016* Return
DM HY Corporates	▲	● Neutral	● Supportive	● Neutral	● Neutral	Lower interest rate sensitivity. Deterioration in credit quality may reverse	13.0%
Asia USD Credit	◆	● Neutral	● Supportive	● Neutral	n/a	Defensive. Stabilisation in China's growth and strong local demand are supportive	5.6%
DM IG Corporates	◆	● Not supportive	● Neutral	● Neutral	● Neutral	Favoured route to take high quality bond exposure	4.6%
EM USD Sovereigns	◆	● Not supportive	● Neutral	● Supportive	n/a	Inexpensive spreads, but rising US Treasury yields and US trade policy risks	9.4%
EM Local Currency	◆	● Supportive	● Neutral	n/a	● Not supportive	Attractive carry, but offset by the risk of USD strength and investor outflows	9.6%
DM IG Govt	▼	● Not supportive	● Neutral	n/a	● Neutral	Fiscal stimulus and Fed rate hikes to lead to rise in yields and decline in prices	3.0%

Source: Bloomberg, Standard Chartered; * Total returns calculated from previous Annual Outlook (11 Dec 2015) to 9 Dec 2016

Legend: ▲ Most preferred | ▼ Least preferred | ◆ Core | ● Not supportive | ● Neutral | ● Supportive

KEY CHART

Figure 1: Bond preference in a rising yield environment



Source: Standard Chartered

CORPORATE CREDIT TO OUTPERFORM GOVERNMENT BONDS

There and back again – The story of 2016

As we look forward to 2017, there is a sense of déjà vu as we see a number of similarities to the time when we were writing the 2016 outlook.

We entered 2016 viewing bonds as an integral part of a balanced investment allocation and a hedge against downside risks. During the year, we upgraded bonds to our most favoured asset class in light of rising risks. The view worked well as the 10-year US Treasury yield declined by nearly 90bp from 2.27% in January to 1.36% in early July and bonds delivered high single-digit to double-digit returns.

However, US Treasury yields rose sharply after the US presidential elections on expectations of fiscal stimulus which could lead to a greater supply of Treasuries, higher growth and higher inflation. Despite the recent spike in yields, our favoured bond sub-asset classes – DM High Yield bonds, DM IG corporate bonds and EM USD government bonds– have performed well (see page 79).

Looking forward to 2017, the risk of higher inflation and Fed rate hikes make us revert to advocating bonds being an important part of a balanced investment allocation rather than a preferred asset class.

Government bonds – Developed Market

DM IG government bonds are our least favoured sub-asset class within bonds; we prefer to take high quality bond exposure through DM Investment Grade corporate bonds instead.

In our opinion, markets have largely re-adjusted to incorporate the expected impact of fiscal stimulus. However, DM IG government bonds are among the most negatively impacted financial assets in an environment of higher growth and inflation, as higher yields can lead to a drop in bond prices by more than the yield on offer, which remains relatively low.

In 2017, the downside risk to US Treasuries arises under both the reflationary scenario and inflationary scenario (see page 11) which would most likely result in higher US Treasury yields. Conversely, the muddle-through and deflationary scenarios are more favourable for bonds as yields are likely to remain rangebound or move lower respectively.

Given our view of 55% probability of higher inflation than today and tighter Fed policy, we expect the 10-year US Treasury yield to rise moderately, closing 2017 between 2.5%-3.0%, assuming the reflationary scenario is confirmed. 10-year bonds have high interest rate sensitivity and when yields rise their price drops more than shorter maturity bond prices. Thus, going into 2017, we favour maintaining a maturity profile centered around 5 years for USD denominated bonds as they offer a balance of lower interest rate sensitivity and moderate yields.

Moving on to other DM IG countries, we believe the Bank of Japan is likely to keep 10-year Japanese government bond yields anchored around 0% and returns are likely to be driven by currency movements. In Europe, the ECB is likely to maintain an easy policy in the near term.

Given our near-term positive stance towards the US Dollar in a reflationary scenario (see page 58), we prefer to keep FX exposure hedged in DM IG government bonds.

Government bonds – EM USD government bonds

We dial back our preference for EM USD government bonds and move them to a core holding.

Some of the key positives remain in place

- an attractive yield of over 5.5%
- inexpensive valuations which remain close to long-term average

However, the asset class has higher sensitivity to rising US Treasury yields. Within EM USD government bonds, the HY component has lower interest rate sensitivity compared to the IG component. The risk of higher US Treasury yields, expectations of a stronger USD which could be a headwind for commodity prices going forward and investor flows make us adopt a more cautious stance.

As discussed earlier (see page 17), we believe EM growth has stabilised which could ease the downward pressure on credit quality. That said, concerns about impact of any potential trade restrictions on EM growth have increased.

The increase in risks leads us to believe the risk/reward has become more balanced. We favour maintaining diversified exposure to EM USD government bonds.

EM local currency government bonds

In line with our slightly reduced optimism for EM assets, we lower our preference to EM local currency government bonds.

As highlighted earlier, stronger growth and an upward bias for commodity prices is a positive, at present. However, a stronger US Dollar is the key headwind for international investors whose impact is transmitted through three main channels:

- Stronger USD reduces total returns for international investors as bonds are denominated in local market currencies

Figure 2: EM USD government bonds are slightly cheap compared to 10-year average

EM USD government bond spreads (yield premium)

Source: Bloomberg, Standard Chartered

EM USD government bonds offer the most diversified exposure to EM debt.

- A weaker local currency may incentivise central banks to ease policy less or, in extreme cases, increase policy rates. An increase in bond yields equates to a decline in bond prices.
- Expectations of the above two factors may lead foreign investors to withdraw money from EM local currency bonds, leading to further price weakness.

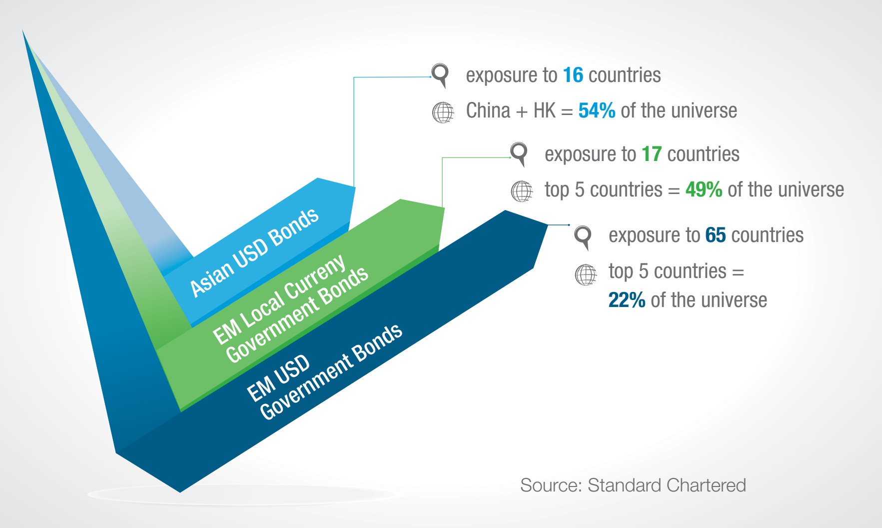
For international investors, gains through bond coupons could be wiped out if the USD strengthens by 6%-6.5% versus EM currencies (see Figure 1 on page 40).

Bond markets of countries with high foreign investor participation and low yields are likely to be more vulnerable versus countries with higher yields. Within Asia, Indonesia (37%) and Malaysia (51%) stand out as the countries which have high foreign investor participation in local currency government bonds.

IDR bonds are vulnerable to a stronger USD and high foreign participation. Additionally, the six rate cuts (totalling 150bps) this year mean we are closer to the end of Indonesia's easing cycle, reducing the potential for further capital gains even in local currency terms. We believe the risk/reward here is not compelling anymore.

Corporate bonds – DM IG corporate bonds

We close our strong preference for DM Investment Grade corporate bonds, given their high sensitivity to interest rate increases. However, they remain our favoured route of taking high quality bond exposure. Within DM IG corporate bonds, we have a favourable bias towards US over European IG corporate bonds as they offer an approximately 2% higher yield.



Source: Standard Chartered

US IG corporate bond returns are driven by both movements in Treasury yields as well as the yield premium* on offer. DM IG corporate bond yield premiums have reduced this year, leading to lower scope for them to reduce further. As an illustration, it would take only a 50bp rise in yields to wipe out the 3.3% yield on offer.

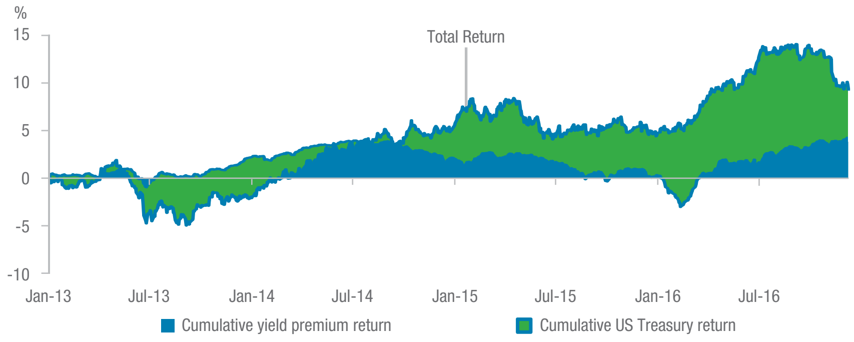
The stronger growth we anticipate, would likely lead to higher revenues for corporates. This should lead to better debt repayment ability and hence an improvement in credit quality. However, it would also lead to higher bond yields, offsetting some of the benefits of reducing yield premium.

On balance, we believe the risk of higher inflation and lower yield premium compared to mid-2016 reduce the relative attractiveness of DM IG corporate bonds and thus we dial back our preference.

*Credit yield premium is the extra yield offered by corporate bonds over the US government bond yield.

Figure 3: US IG corporate bond returns are driven by both Treasuries and spreads (yield premium)

Breakdown of total return from US IG Corporate bonds



Source: Barclays, Bloomberg, Standard Chartered

Corporate bonds – DM HY corporate bonds

DM High Yield corporate bonds and US floating rate loans are now our most preferred sub-asset classes as we believe they are best positioned in a reflationary environment. We like their:

- Lower interest rate sensitivity
- Contained default risk
- Exposure to improving global growth outlook
- Higher correlation to equities

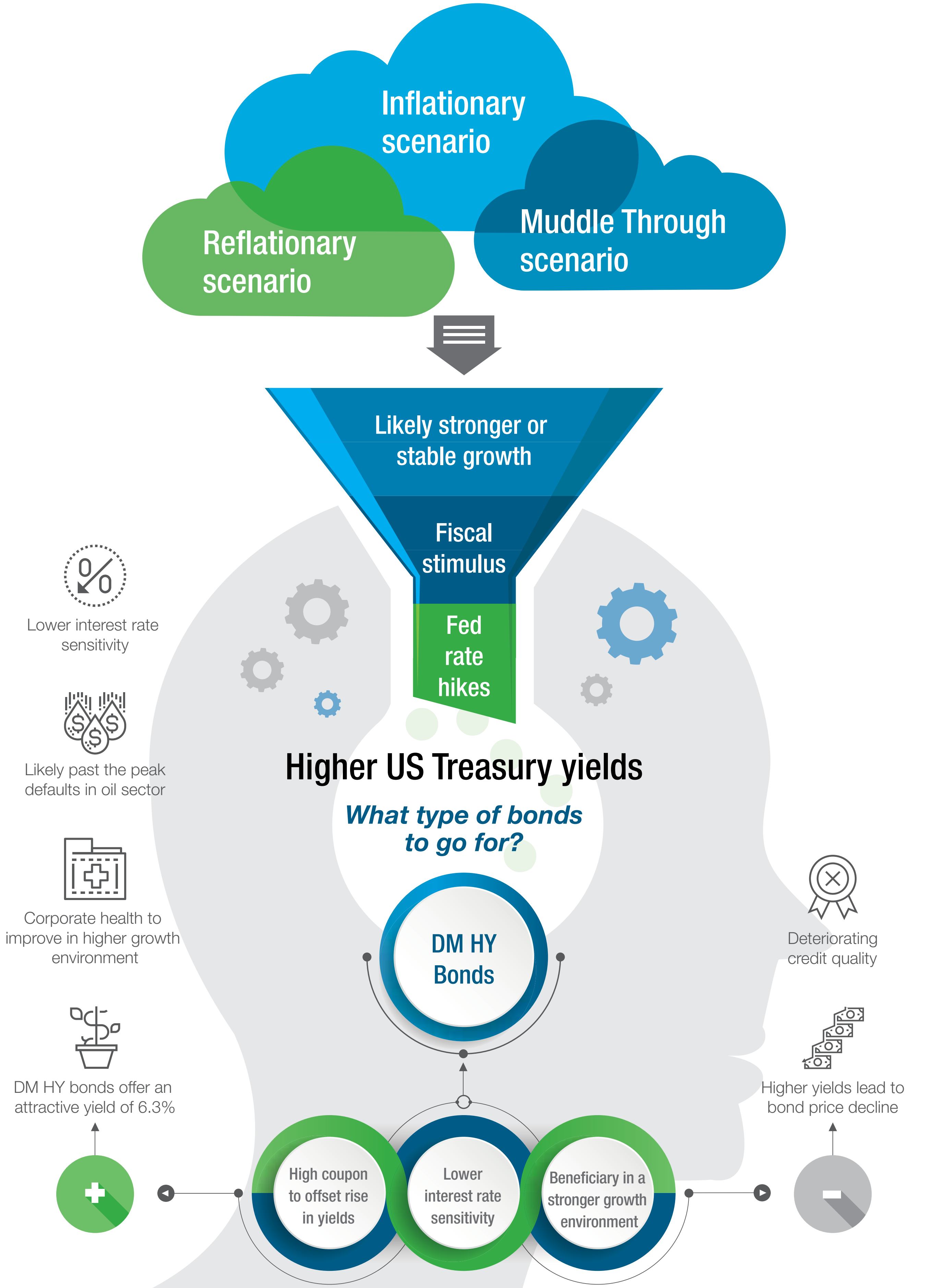
While we view both options positively, we favour US floating rate senior loans over DM HY corporate bonds as they offer an attractive and lower risk option to gain exposure to debt from high yield companies. They have very low interest rate sensitivity as they offer coupons linked to short-term interest rates. The coupons are reset every 3 months and would increase if rates move higher. Thus, they tend to be more resilient in a rising interest rate environment and exhibit lower volatility, albeit for a slightly lower yield. Their secured nature gives us additional comfort as they are likely to be more resilient towards the end of credit cycle.

Within HY bonds, we have a bias for US HY bonds over EUR HY bonds as the former offer higher yields (US HY: 6.5% vs European HY: 4.1%) and are likely to benefit from higher growth in the US. Our positive view on oil prices leads us to believe that peak defaults from energy companies are largely behind us. Though defaults from other sectors could rise, we believe that, absent an economic shock, overall default rates are likely to trend lower; major rating agency estimates suggest default rates could trend lower from nearly 6% in 2016 to below 4% in 2017.

We acknowledge headline credit quality is still on a downward trend as companies have progressively taken on more debt and become more leveraged. However, low interest rates mean their debt servicing ability has not deteriorated sharply. Stronger US economic growth would likely lead to higher revenues and debt repayment ability, offsetting the rise in financing costs in case yields move higher.

A failure of growth to pick up, accompanied by a rise in inflation (i.e. stagflation, 20% probability) is the key downside risk to US HY bonds. Such a scenario would lead to higher funding costs and lower profitability, and possibly deterioration in credit quality.

Why do we prefer DM HY bonds?



Corporate bonds – Asian credit

We remain comfortable holding Asian USD bonds as we continue to like their defensive characteristics within EM bonds. Within this segment, we prefer IG corporate bonds over HY corporate bonds, when balancing potential returns with the risks.

Asian corporate bonds benefit from a strong regional investor base, which has led to lower volatility compared to other Emerging Markets and even DM IG government bonds over last few years. While this trend has been a major positive for Asian USD bonds, a reversal at some point is likely. This tempers our enthusiasm somewhat for the asset class.

The increasing participation from regional investors as well as reports suggesting international investors are underweight Asian USD bonds are a positive. The depreciation of CNY has led to greater demand for USD-denominated assets from Chinese investors. Our key assumption is this trend will remain in place (see page 62).

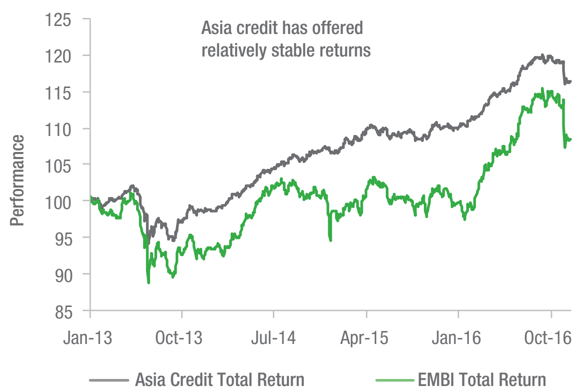
Supply is expected to remain high as issuers refinance large amounts of upcoming maturities in 2017. Chinese issuers could become even more dominant constituents in the universe, leading to higher concentration risk. Bonds of issuers from mainland China and Hong Kong currently account for nearly 54% of all Asian USD bonds and this number is likely to rise in 2017.

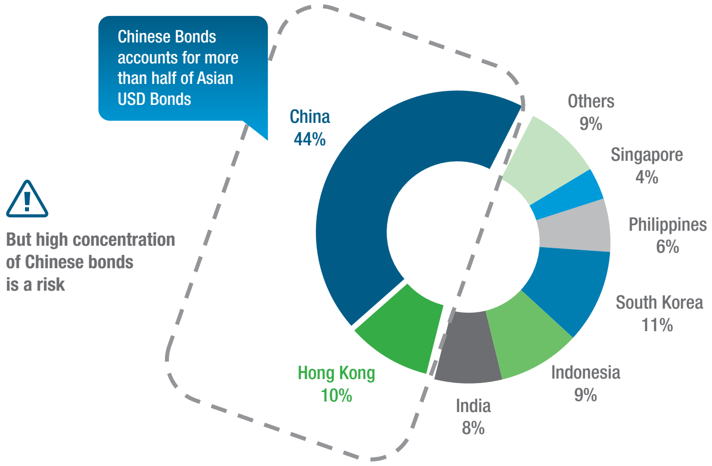
China undoubtedly faces a challenging task of supporting growth and managing its high level of debt. Given our stable view about Chinese fundamentals over the next 12 months (see page 17), we believe there is a low likelihood of a sustained risk spike due to concerns of a hard landing. However, such an eventuality could lead to a disproportionate negative impact on Asian USD bonds, given the high concentration of Chinese issuers.

There is also significant divergence in credit fundamentals. Credit quality of IG corporates has been improving marginally whereas it has been on a deteriorating trend for high yield corporates. The low yield premium and deteriorating credit quality lead to a less favourable risk/reward for high yield corporate bonds.

Figure 4: Asian USD bonds have been more defensive compared to broad EM USD government bonds

Asia Credit and EMBI cumulative total returns. Rebased to 100 on 1 Jan 2013





Source: JP Morgan, Bloomberg, Standard Chartered

KEY INVESTMENT THEMES AT A GLANCE

1 Corporate bonds to outperform government bonds

2 DM High Yield bonds to outperform broader bond universe

3 US floating rate senior loans to deliver positive returns

EQUITY
AT A GLANCE

[Clive McDonnell]

KEY THEMES

We are more positive on the outlook for equity markets as we head into 2017. On a relative basis the US is our most preferred equity market driven by expectations of a recovery in corporate earnings.

The UK is our least preferred equity market due to concerns about weak corporate margins and expensive valuations at a time of considerable uncertainty over the outlook for the corporate sector.

Our scenario-based analysis signals a combination of reflationary upside and muddle-through as the most likely scenarios as we enter 2017. This is a change from our prior scenario which focused on a muddle through environment.

While the potential for rising inflation has recently become a source of concern among investors, this is not necessarily a threat to equity markets. We observe that rising inflation is linked with rising corporate margins.

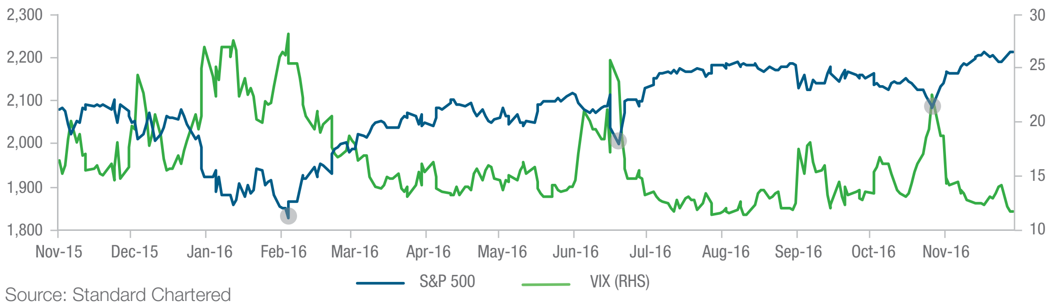
KEY DRIVERS

Equity	US	Euro Area*	UK	Japan*	AxJ	Non-Asia EM	Comments
View	▲	◆	▼	▲	◆	◆	
Earnings Revisions	🟢	🟢	🟢	🟢	🟢	🟢	Earnings revisions are a short term momentum indicator that drive equity markets
Earnings	🟢	🟢	🟢	🟡	🟢	🟡	Earnings are a key driver of equity markets
Return on Equity	🟢	🟢	🟢	🟢	🟡	🟡	Return on equity is a long term driver of shareholder value
US Economic Data	🟢	🟡	🟡	🟢	🟢	🟡	Both the US and other markets can react to US economic data based on economic linkages
Local Economic Data	🟢	🔴	🟢	🟢	🟢	🟢	Local economic data acts as driver of equity markets with the exception of the euro area
Bond Yields	🟢	🟢	🟢	🔴	🟡	🟡	Bond yields are a key driver of equity markets with the exception of Japan
Liquidity	🟡	🟡	🟡	🔴	🟢	🟢	Liquidity is a key driver of equity markets with the exception of Japan

Source: Standard Chartered. *FX-hedged exposure
Legend: ▲ Most preferred | ▼ Least preferred | ◆ Neutral | 🔴 Not a driver | 🟡 Sometimes a driver | 🟢 Frequently a driver
Note: The colour of each signal refers to its relevance as a driver as opposed to its current positive/ neutral/ negative status.

KEY CHART

Figure 1: A buy on weakness strategy worked in 2016 and may work again in 2017



Source: Standard Chartered

LATE CYCLE, NOT END OF CYCLE

Earnings recovery, fiscal stimulus, lower corporate taxes, euro and yen weakness are all positive catalysts for equity markets as we enter 2017.

Catalysts for global equity markets:

- **Earnings recovery:** consensus expectations for Developed Market (DM) earnings growth in 2017 is 12%, a significant acceleration from the 1% recorded in 2016.
- **Fiscal stimulus and investment recovery:** President-elect Trump looks set to boost infrastructure spending and cut corporate taxes in 2017.
- **Euro and yen weakness in 2017:** potential positives for Euro area and Japanese equities, noting the need to hedge FX exposure.

Risks for global equity markets:

- **Rising rates and a strong dollar:** rising US interest rates and a strong US dollar are risks to Emerging Markets (EM), in particular Asia ex-Japan as it tightens financial conditions in the US and drains liquidity from the region.
- **Trump effect reverses:** US equity markets have rallied and bonds have slumped as investors digest the implications of President-elect Trump's policy agenda. If compromises with the Republican Party significantly dilute his proposals, expect equity and bond markets to refocus on the muddle through scenario.
- **European political calendar:** European voters go to the polls to cast their votes in elections in Germany, France and Netherlands in 2017.

Greater conviction over the likelihood of a recovery in US corporate earnings to 12% growth in 2017 from 1% in 2016 has led us to upgrade the outlook for US equities. A recovery in corporate earnings signals an extension in the economic cycle, potentially closer to that observed in the 10-year period between 1991-2001 as opposed to the average seven year cycles observed since 1970.

Our central scenario is for modest US dollar strength which, in combination with the risk of a retreat from the globalisation trend of the past 22 years is a headwind for Emerging Markets (EM).

Our most preferred markets as we enter 2017 include US, Japan (on a FX-hedged basis) globally, and India and Indonesia in Asia.

U.S.

Twin drivers – earnings and bond yields

Key drivers of our view include:

- The US is our most preferred equity market as we enter 2017. Our assessment of the outlook for US equities has improved, driven by a shift in expectations with regard to corporate earnings.
- An added factor supporting our positive view on US equities is an improvement in the outlook for corporate margins.
- Rising US interest rates are a risk to the recovery, but assuming earnings expectations continue to be revised higher at the same pace or faster than the cost of capital, the equity market can continue to perform.

US equities: Our most preferred market as we enter 2017

The outlook has improved, driven by a shift in expectations with regard to corporate earnings. Previously, we focused on the potential for a recovery in corporate earnings driven by a single sector: energy. However, we have recently witnessed a much broader improvement in the earnings outlook in the market. This is signalled via the earnings revision index, which has seen a significant improvement since September 2016.

Earnings expectations in the banking sector in particular have improved as analysts raise earnings forecasts driven by the positive impact of higher bond yields on net interest margins. Bank earnings are forecast to rise 7% in 2017, following a 1% contraction in 2016.

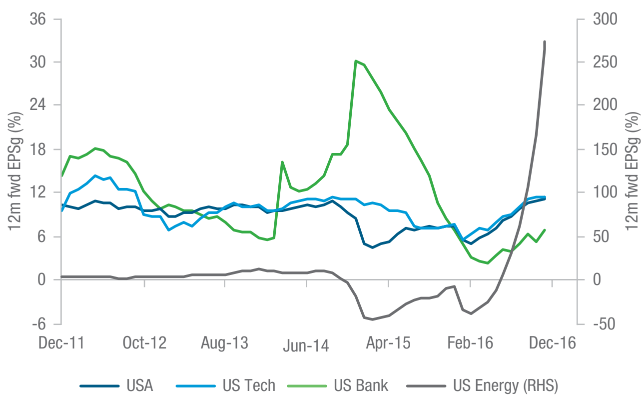
US corporate earnings are forecast to increase 12% in 2017 after 1% growth in 2016

An added factor that is supporting a more positive view on US equities is a change for the better in the outlook for corporate margins.

US margins had been under pressure due to lacklustre demand and intense competition keeping prices in check. However, there has been a change in the outlook for prices in recent months as reflected in an uptick in inflation expectations. This is a potentially significant development as there is a relationship between corporate margins and the ratio of planned price hikes and worker compensation as reflected in Figure 3.

Figure 2: US earnings recover, led by energy

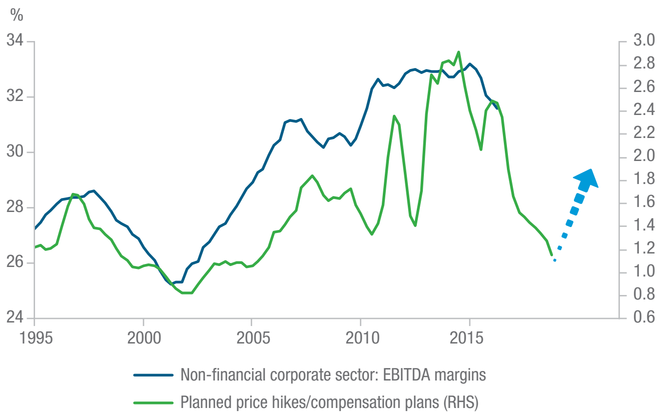
US earnings growth expectations



Source: Standard Chartered, Bloomberg

Figure 3: US margins and planned price hikes

If price hikes outpace wage increases, margins could expand



Source: Bureau of Economic Analysis; Bloomberg, Standard Chartered
Note: Non-financial corporate sector: EBITDA margins (4-quarter moving average)/planned price hikes/compensation plans (12-month moving average), advanced by 3 years

Higher US margins could help drive up the return on equity, supporting what we characterise as an elevated, but not overvalued equity market which trades on 17 times 2017 forecast earnings. This is, in turn, supportive of an extended market cycle assuming rising interest rates do not overtake rising growth expectations.

Our position in the economic cycle and the length of the cycle has significant implications for returns. We are eight years from the trough in the prior cycle. If we assume the current cycle will be similar to the ten year 1991-2001 cycle as opposed to the average seven year cycles observed since 1970 (excluding the short lived 1980-1981 cycle), the potential average annual return over the next two years is 10%.

Another positive catalyst for the US market is the potential for lower taxes

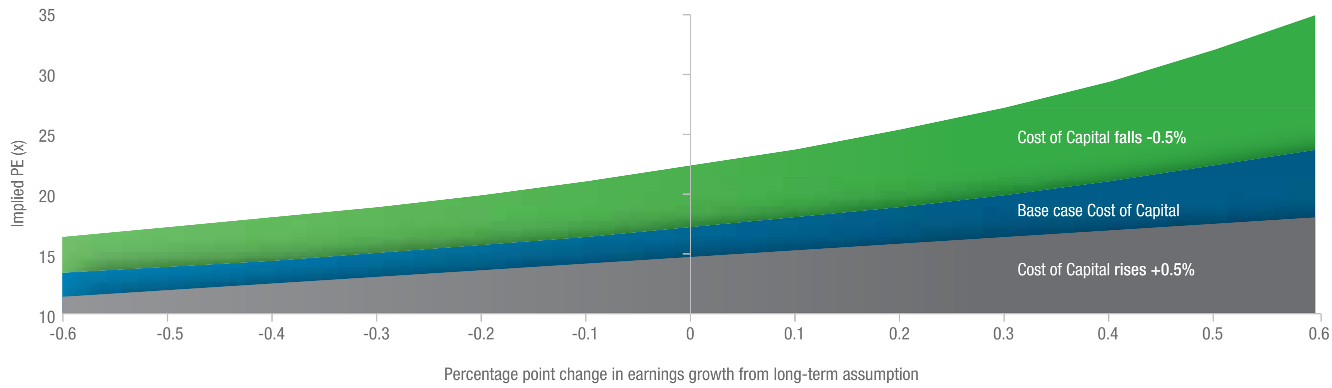
The top rate of US Federal corporate tax is currently 35% with an effective tax rate of 25%. If this were to fall, and the new administration encouraged the return of the estimated USD2.6 trillion of US profits held overseas, it could result in an increase in share buybacks, dividends and investment; all of these are positive for corporate earnings.

Rising US bond yields are a risk to the recovery

As long as expectations for long term earnings growth remain above long term estimates for the cost of capital, the equity market can continue to perform. Current long term implied earnings growth in the US is 4.3%. Implied long term earnings growth needs to rise to 5.2% for the US equity market to maintain its current valuation assuming the cost of capital rose to 7.4%.

Figure 4: Lower cost of capital boosts valuations and vice versa under different earnings growth rate assumptions

Sensitivity of US valuations to long term growth rate



Source: Bloomberg, Standard Chartered

Japan

Yield curve and the yen are key

Key drivers of our view include:

- The Japanese equity market is attractive based on near double digit-earnings growth in 2017 and reasonable valuations relative to history.
- Reflecting the greater focus on shareholder returns in Japan and increased dividend payouts, we have witnessed an improvement in the return on equity, rising from 8% in 2015 to a forecast 9% in 2017.
- The yen is a key driver of the Japanese equity market. A weak yen is a positive driver of sectors such as industrials and consumer discretionary.

Japanese equities: Our second most preferred global equity markets on a FX-hedged basis
The market is attractive based on near double digit-earnings growth in 2017 and reasonable valuations relative to history. However, prior policy mis-steps by the Bank of Japan (BoJ) and uncertainty over the outlook for the banking sector are fresh in investors minds and create uncertainty.

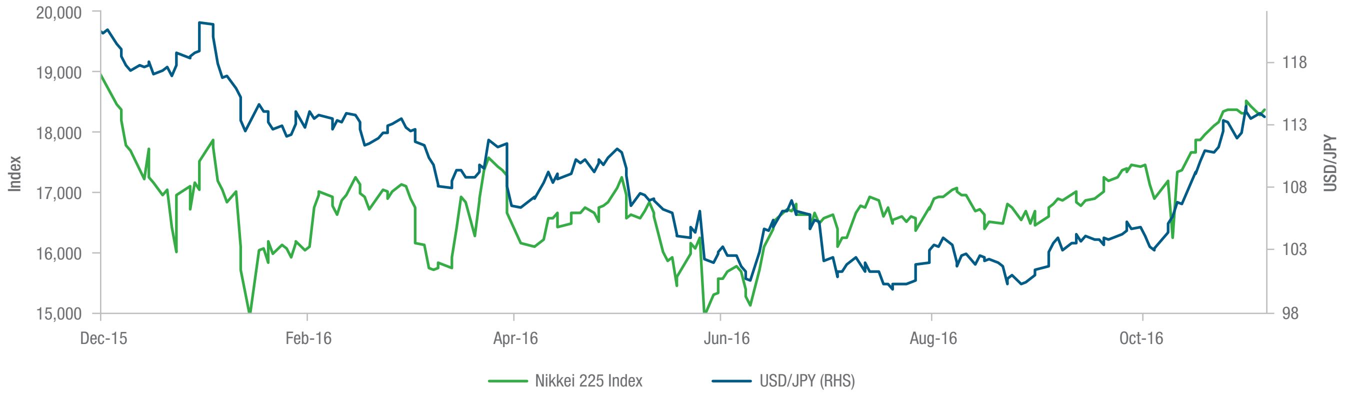
The performance of the Japanese banking sector has improved since the BoJ's policy of yield curve control (YCC) was announced, but earnings have yet to catch up. Current expectations are for a 6% contraction in Japanese bank earnings in 2017.

The Japanese industrials sector is a prime beneficiary of a weak currency and a pick up in fiscal stimulus globally. Consensus expectations are for 19% growth in the industrials sector earnings growth in 2017, contributing almost a third of headline index earnings growth.

Reflecting the greater focus on shareholder returns in Japan, we have witnessed an improvement in the return on equity, rising from 8% in 2015 to a forecast 9% in 2017.

Investors should focus on sectors such as industrials and consumer discretionary which are beneficiaries of a weak yen. Some exposure to banks is warranted given the potential for upside surprise in earnings given the policies implemented by the BoJ in 2016, including YCC.

Figure 5: Nikkei rises and falls with USD/JPY
Japanese Nikkei index and USD/JPY



Source: Bloomberg, Standard Chartered

Asia ex-Japan

Watch the dollar and flows

Key drivers of our view include:

- We anticipate a recovery in earnings growth amid signs of stability in China. However, the impact of US dollar strength remains a risk.
- Earnings growth in Asia ex-Japan is forecast to rise to 12% in 2017 from 2% in 2016.
- As we enter 2017, India and Indonesia are our most preferred markets within Asia ex-Japan; Malaysia and Singapore are our least preferred.

We are neutral on Asia ex-Japan as we enter 2017
Positives include a recovery in cyclical sectors relative to defensives and the outperformance of banks in China. Negatives include dollar strength and the threat to continued growth in global trade.

Earnings growth in Asia ex-Japan is forecast to rise to 12% in 2017 from 2% in 2016, led by a recovery in China and Taiwan. While this is a clear positive trend, we note that in contrast to DM, earnings revision for Asia ex-Japan, while recovering from their lows, remain negative.

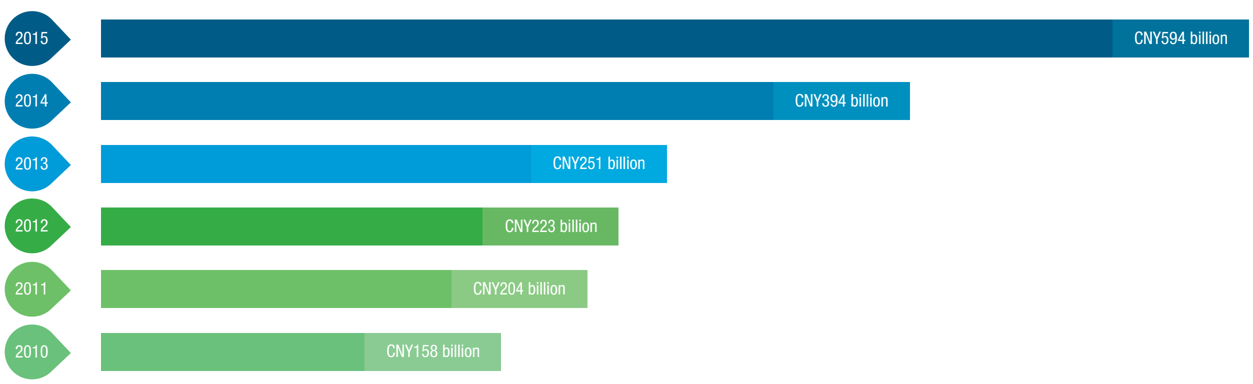
The most likely factor restraining analyst earnings forecasts is concern over a strong dollar, which in turn is driven by rising US bond yields. While fundamentals in Asia are much improved from 2013, when we last witnessed a rise in US bond yields, there remain vulnerabilities in selected economies including Indonesia and Malaysia. Specifically, we see elevated levels of foreign currency debt and high levels of foreign ownership in the local currency bond market.

US dollar strength acts as a drag on foreign portfolio inflows to Asia
Year-to-date USD21 billion has flowed out of regional equity funds, implying 2016 would be the fourth consecutive year of outflows from the region.

We are positive on the reduction of systemic risk in China driven by the increased recognition of the NPL problem facing the banking sector. This is best captured by the almost four fold increase in listed bank debt write-off's to CNY594 billion from CNY158 billion in 2010, as reflected in Figure 6.

While this has lowered the NPL coverage ratio and negatively impacted bank profits, the sector has actually re-rated as investors cheer the belated recognition of the challenges facing the sector.

Figure 6: Banks have significantly increased their provisioning
Chinese bank provision for loan losses



Source: Bloomberg, Standard Chartered
Note: Aggregate of 16 Commercial Banks listed in A-Share market

India – demonetisation shock

India is one of our most preferred markets as we enter 2017 despite the demonetisation shock. Consensus expectations for earnings growth is for 17% in 2017. PE valuations have recently declined from over 18 times 2017 forecasts to just over 16 times.

Indonesia – dollar strength worries

Indonesia is also amongst our most preferred equity markets. Earnings growth of 15% and a pick-up in infrastructure investment are positives. US dollar strength has recently negatively impacted the Indonesian market as investors fret about the impact of rising foreign currency debt servicing costs. We expect this to be short lived.

Malaysia – outlook remains challenging

Malaysia is one of our least preferred markets as we enter 2017. The market has been impacted by slowing earnings growth and sharp slowdown in headline economic growth due to weakness in investment and consumption related to the uncertain political environment. We remain watchful for any signs of a recovery, including an end to the political uncertainty and/or a pick-up in corporate investment.

Singapore – trade woes

Singapore is also one of our least preferred markets. As the most open economy in Asia, lacklustre global trade has weighed heavily on growth. Weakness in the oil and gas sector has also weighed on the market. Rising bond yields are a positive for the banks and, similar to Malaysia, we remain watchful for signs of a recovery including a pick up in new orders in the oil and gas industry and/or a recovery in bank net interest margins.

Euro Area

Weak euro to boost industrials

Key drivers of our view include:

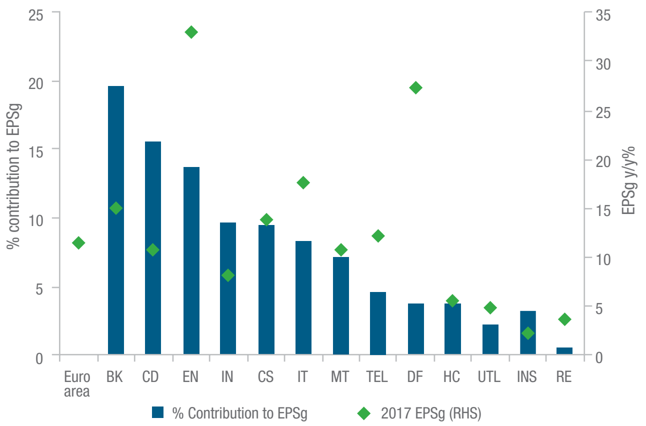
- Euro weakness and the positive effect on corporate earnings. Consensus expectations for earnings growth in the Euro area is 12% growth in 2017.
- We are hopeful that the banking sector can put its recent challenges behind it, but there remain risks in the sector.
- Investors in Euro area equities in 2017 need to be mindful of parliamentary and presidential elections in France and Germany as well as a general election in Netherlands.

We are neutral on Euro area equities on a currency-hedged basis as we enter 2017
The outlook for Euro area economic growth remains challenging. However, we note the positive effect on corporate earnings from a weaker euro. Taken together, these factors drive our neutral view relative to other markets.

Consensus expectations for earnings growth in the Euro area is 12% growth in 2017
One fifth of the increase in earnings is concentrated in the banking sector. This has some risks associated with it due to the impact of low bond yields. Moreover, the sector is not a significant beneficiary of a weaker euro.

Figure 7: Banks contribute one fifth to Euro area EPSg in 2017

Euro area earnings breakdown



Source: Bloomberg, Standard Chartered

Nevertheless, potential positive surprises could emerge. The sector may soon be able to put overhangs including fines from US and EU regulators, which accounted for 40% of earnings in 2016, behind it. The recapitalisation of the Italian banking sector, if completed, would also remove a big uncertainty.

We have greater confidence that the industrial sector could witness a re-rating as investors digest the positive implications of fiscal stimulus in the US and a weaker euro. The industrial sector is the second largest by market capitalisation and is a prime beneficiary of these twin trends.

Reflecting the improvement in the outlook for earnings in the Euro area driven by a weaker euro is the recent surge in the earnings revisions index. This lead indicator is now signalling an improvement in the outlook for earnings in the year ahead. If this trend continues, it represents an inflection point from a fifteen month period of negative earnings revisions, which weighed on the market.

Indicators of corporate margins and, in turn, ROE remain lacklustre in the Euro area, signalling limited upside to current market valuations. Currently, the market trades on 14 times 2017 consensus earnings estimates, which is above its long term average.

One of biggest risks facing Euro area equities in 2017 centres on the election calendar. Parliamentary and presidential elections in France and Germany as well as a general election in Netherlands are potential sources of instability that investors need to monitor closely.

The political calendar poses downside risks to earnings growth in domestically-orientated sectors in the Euro area. However, the equity market is primarily driven by external demand with >50% of sales coming from outside the Euro area. As such, a weaker euro can boost sales and potentially profits, even if domestic demand is weak.

Non-Asia EM

Watch commodity prices

Key drivers of our view include:

- The outlook for non Asia-EM is heavily influenced by commodity prices. We are neutral on commodity prices as we enter 2017, which in turn significantly influences our equity view.
- Earnings growth in non Asia-EM will slow in 2017, albeit from a high base in 2016.
- The outlook for growth in China and the extent to which fixed asset investment could recover will have a significant impact on the outlook for Brazil.

We are neutral on Non-Asia EM as we enter 2017
Drivers of the positive view include our central scenario of 12-month returns from commodity indices of 0-5% and oil prices trending gradually higher from here with a cap at USD60-65.

US dollar strength is less of a risk for non Asia-EM as currencies in Brazil and Russia are undervalued and could benefit from the commodity price recovery.

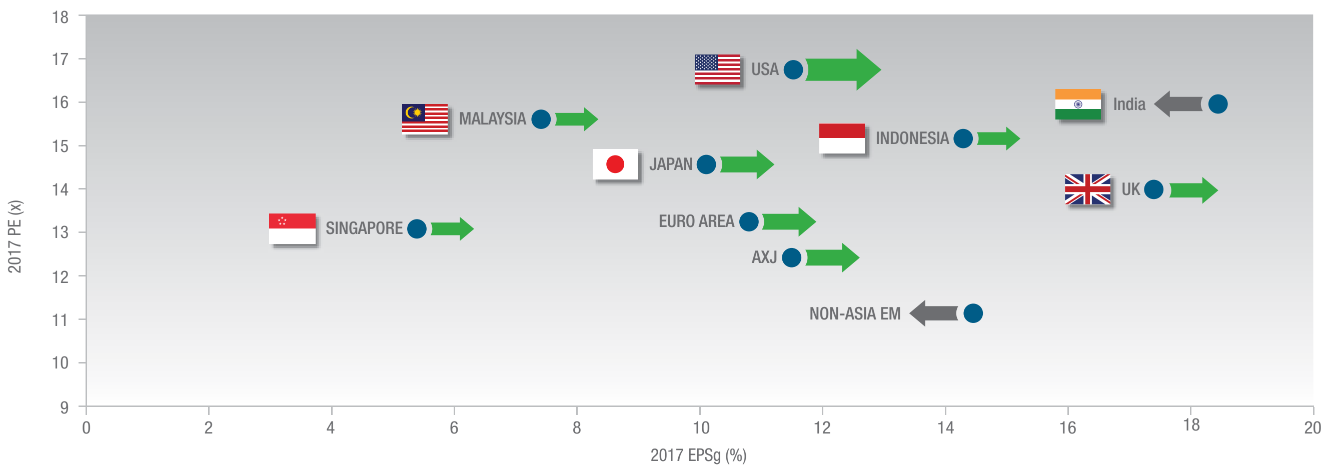
Earnings growth in non-Asia EM will slow in 2017 – one of the two regions/markets where this will occur. Consensus expectations is for earnings growth of 13% in 2017, compared to 25% in 2016.

Admittedly the majority of the slowdown in non-Asia EM earnings is related to weakness in Brazil. This, in turn, is witnessing a normalisation in its earnings growth following a commodity price induced surge in 2016.

The outlook for growth in China is key for Brazil
A reduction in benchmark interest rates from the current 14% and a recovery in the Brazilian real would help boost incomes and, in turn, consumption. Banks are the single largest sector in the Brazilian market and are a beneficiary if these two factors were to act as positive catalysts.

Trading on 11 times 2017 consensus earnings forecasts, valuations in non-Asia EM are elevated. However, this is not a key concern as earnings growth looks set to be revised higher driven by the commodity price recovery.

Figure 8: Non-Asia EM is one of two regions/markets witnessing slower earnings growth
Global markets 2017 earnings growth and valuations



Source: Bloomberg, Standard Chartered
Note: Mid points: 10% 2017 EPSg | Arrow size: The bigger the arrow, the bigger the market capitalisation
Arrow colour: Compare to prior year, ➡ = higher; ⬅ = lower

U.K.

Article 50 uncertainty

Key drivers of our view include:

- The start of the UK's negotiations to leave the EU, or the triggering Article 50, is an overhang for the market.
- Similar to the Euro area, the UK equity market has a much greater dependence on trends overseas, particularly in commodity markets, as opposed to domestic demand.
- The UK's position as an overvalued market when the UK voted in favour of leaving the EU and the subsequent dramatic decline in corporate margins signal a challenging outlook for UK equities in 2017.

The UK is our least preferred market as we enter 2017
The start of the UK's negotiations to leave the EU, or the triggering of Article 50, is an overhang for the market. However, similar to the Euro area, the UK equity market has a much greater dependence on trends overseas, particularly in commodity markets, as opposed to domestic demand.

As such, while uncertainty over negotiations on withdrawal from the EU could act as a drag on domestic consumption, this does not necessarily translate into weakness in the equity market.

Despite these potential offsets, the UK's position as an expensive market when the UK voted in favour of leaving the EU and the subsequent dramatic decline in corporate margins signals a challenging outlook for UK equities in 2017.

While corporate earnings are forecast to increase by 20% in 2017 compared to 3% growth in 2016, this is primarily a function of 17% decline in sterling since the Brexit vote and the increase in commodity prices. The energy and materials sectors represent a fifth of the index market capitalisation, but account for almost two thirds of expected earnings growth in 2017.

UK non-financial corporate margins, which are more reflective of underlying corporate health, have slumped to 3.6%. This compares to 8.5% in the US and 5% in the Euro area.

Investors in the UK should focus on external and commodity linked sectors. Including energy, materials and consumer discretionary to hedge against the risk of slower growth associated with weaker domestic demand as the UK disentangles itself from the EU.

Figure 9: UK is expensive relative to its own history

UK market price-earnings ratio

Source: Bloomberg, Standard Chartered

THEMATIC VIEWS

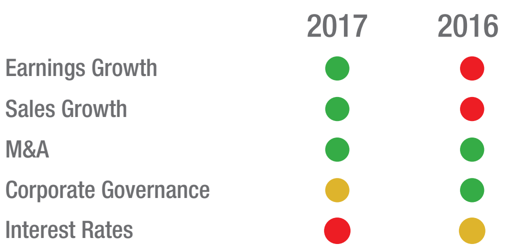
We have three thematic views as we enter 2017: US technology, US small cap and new economy sectors in China.

US SMALL CAP

Strong Dollar Beneficiary

US small caps are a new conviction view as we enter 2017. Drivers of US small caps are highlighted below, which compares their current position with the position 12 months ago. Small cap companies are also potential beneficiaries of tax reform, in particular proposals to lower the headline rate of corporate taxation. A strong US dollar also benefits small cap relative to large cap due to their greater focus on domestic growth.

US small capitalisation stock drivers
Drivers signalling green have increased relative to 2016



US TECHNOLOGY

Tax Beneficiary

US technology is a conviction view as we enter 2017. Drivers of the view include growth in demand for cloud services driving earnings of large technology companies. The sector may be a prime beneficiary of proposed US tax reform, in particular any change in the tax treatment of profits held overseas. If this cash is repatriated, it could be used for share buy backs and dividends as well as increased capital expenditure.

CHINA: NEW ECONOMY

Focus on e-Commerce

China: new economy is a new conviction view as we enter 2017. We believe demographics, urbanisation and the trend towards greater use of the mobile internet are drivers of faster growth in new economy sectors. These include technology and services. Earnings growth and valuations are higher in these sectors compared to the broader market. Higher corporate margins supports the higher valuation in our view.

KEY INVESTMENT THEMES AT A GLANCE

1 US equities: Our highest conviction market as we enter 2017

2 Japan (FX-hedged) a conviction market as we enter 2017

3 India and Indonesia are our Asian market conviction views as we enter 2017

4 We have three high conviction thematic view as we enter 2017: US technology, US small caps and China new economy sectors

FX
AT A GLANCE

[Tariq Ali, CFA | Manpreet Gill]

KEY THEMES

We expect moderate USD strength going into 2017. We expect weakness in the EUR, JPY, GBP and CNY heading into 2017 amid higher expectation of US interest rates and continued policy easing by the respective central bank. Our highest conviction views are short EUR/USD and long USD/CNY.

We expect the AUD and NZD to extend gains in 2017. We expect strength in the AUD and NZD against the backdrop of rising inflation, higher commodity prices and the likely absence of further easing from the local central banks. Our highest conviction view is long AUD/USD.

Selective currency performance within Emerging Market currencies. We expect commodity linked currencies with improving balance of payment fundamentals and high interest rates (RUB, BRL, IDR and INR) to outperform other Emerging Market currencies against the USD.

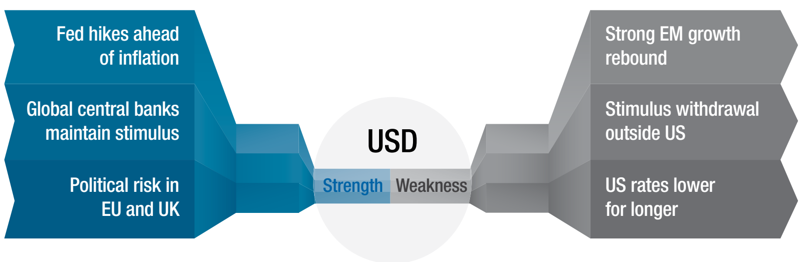
KEY DRIVERS

Currency	Outlook	Real Interest Rate Differentials	Risk Sentiment	Commodity Prices	Broad USD Strength	Comments
USD	▲	Supportive	Supportive	Not Supportive	n/a	Higher US rates coupled with maintenance of policy easing in major economies
EUR	▼	Not Supportive	Not Supportive	n/a	n/a	Widening rate differentials as ECB maintains easy policy settings
JPY	▼	Not Supportive	Neutral	n/a	n/a	Widening rate differentials amid BoJ's yield curve control policy
GBP	▼	Not Supportive	Not Supportive	n/a	n/a	Weak sentiment amid post Brexit uncertainty and weak balance of payment fundamentals
AUD, NZD	▲	Neutral	Supportive	Supportive	Not Supportive	Moderately higher commodity prices to be supportive while easing cycle has likely troughed
EM FX	◆	Not Supportive	Supportive	Supportive	Not Supportive	Modestly stronger USD is a headwind, but moderately higher commodity prices and stable China growth to limit downside

Source: Bloomberg, Standard Chartered
Legend: ▲ Bullish | ▼ Bearish | ◆ Neutral | ● Not Supportive | ● Neutral | ● Supportive

KEY CHART

Balance of factors still supportive of USD strength. However, this depends a lot on how the Fed responds to resurgent inflationary pressures



Source: Standard Chartered

FED OUTLOOK KEY

USD: Riding on higher US rate expectations

In 2016, the USD (trade weighted) stalled as Fed rate hike expectations were scaled back owing to lacklustre US growth and inflation expectations. Recently, USD gains resumed following the US elections amid increased fiscal stimulus expectations and a surge in US yields. A reflationary or a high inflation scenario (55% probability, see page 11) would be positive for the USD as long as Fed rate hikes do not underwhelm market expectations. We expect a range-bound outcome in a muddle-through scenario.

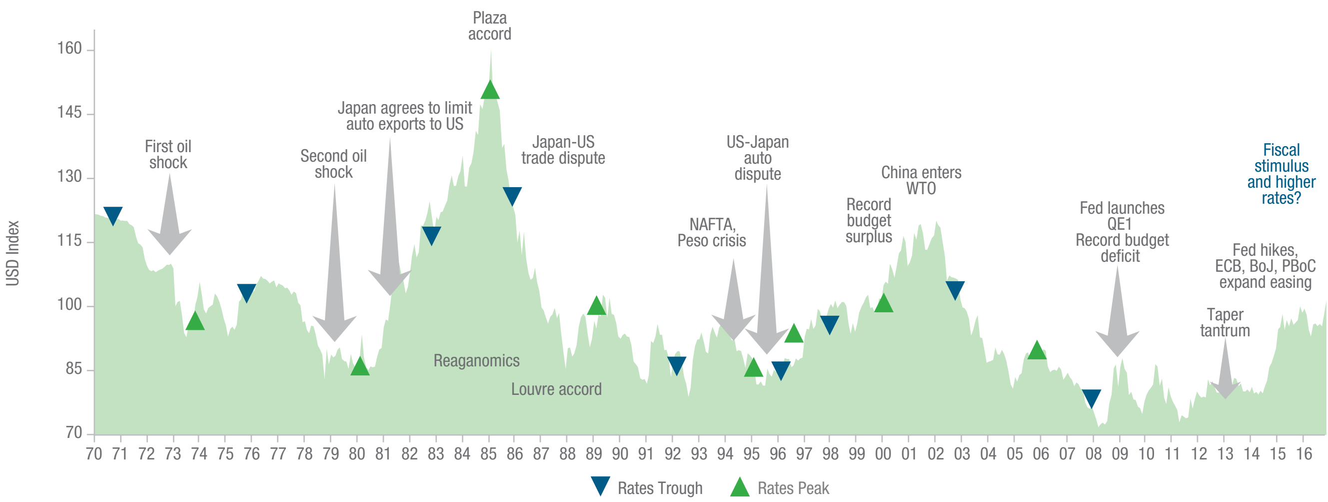
We believe the USD could modestly extend gains into early 2017, in our base case, predicated on two assumptions. First, in response to higher inflationary pressures, the Fed proactively hikes interest rates while most other central banks and, in particular, the BoJ, ECB, BoE and at least PBoC at least maintain their current accommodative policies. This would likely widen net-of-inflation (real) interest rate differentials in favour of the USD. Second, while we expect EM growth to stabilise, a strong rebound remains unlikely and, hence, sentiment towards them remains cautious. A significant part of the USD trade-weighted index is constituted of EM currencies.

We see two major risks to our outlook for modest USD strength in 2017. First, the Fed could adopt an objective of allowing inflation to move above its target for a certain period (sometimes referred to as running a 'hot' economy). This would narrow real interest rate differentials and weaken the USD. Second, Emerging Markets stage a strong rebound, attracting increased capital flows and weakening the USD.

A reflationary or a high inflation scenario would be positive for the USD as long as the Fed stays at least in line with its rate hike expectations. Expect a range-bound outcome in a muddle-through scenario.

Figure 1: A historical perspective of the USD through US rate cycles, trade events, financial crises and fiscal expansions

USD Index



Source: Bloomberg, Standard Chartered

EUROPEAN EURO

Short term | Medium term

EUR: Political risks could dominate

The EUR/USD has traded in a relatively tight range (largely 1.05-1.15) over the past two years. However, we believe the EUR is likely to break lower in 2017.

Outside of the broad USD trend, two key factors shape our EUR outlook. First, ECB monetary policy and second, Euro area political risks. On the first point, our base case is that the ECB retains its loose policy settings in order to entrench inflation expectations. This is likely to keep real yields in Europe low, while those in the US continue to increase. On the second point, markets are likely to become increasingly focused on the risk of populist/Eurosceptic political parties in the Euro area following Brexit and the US elections. The main risk to our view of a weaker EUR is the ECB switches its policy to a less accommodative stance and begins to significantly scale-back asset purchases. This risk is likely to increase as we move through 2017 if reflation takes hold globally.

JAPANESE YEN

Short term | Medium term

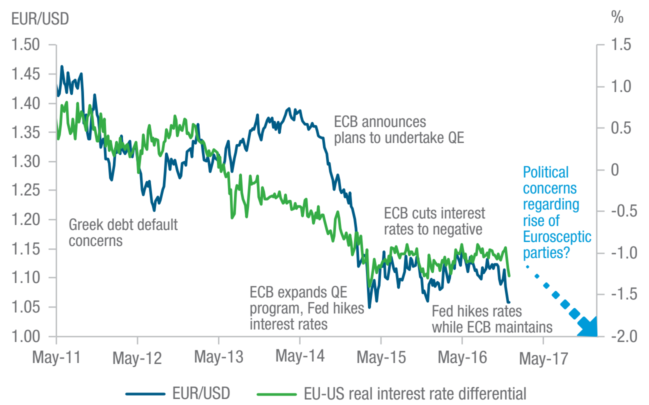
JPY: US interest rate outlook key

The JPY strengthened significantly in 2016 amid limited success by the BoJ to lower (net of inflation) Japanese interest rates. The JPY, however, gave up half its gains following the surge in the USD near year-end. We believe JPY can further weaken moderately in 2017.

With the BoJ capping 10-year Japan yields, the JPY outlook for 2017 depends to a significant extent on the outlook for US yields. With the Fed likely to hike rates at least 2 times in 2017, a widening of US-Japan real interest rate spreads could exacerbate capital outflows from Japan and weaken the JPY. We see two main risks to this outlook. First, should Japan inflation continue to fall, it could increase real interest rates in favour of a stronger JPY. Second, higher global risk aversion or a significant pick-up in trade disputes would be supportive for the JPY as Japan remains a significant net-lender to the rest of the world.

Figure 2: With the ECB likely to maintain current easing policy for now, real interest rate differentials are expected to fall further amid higher US rates

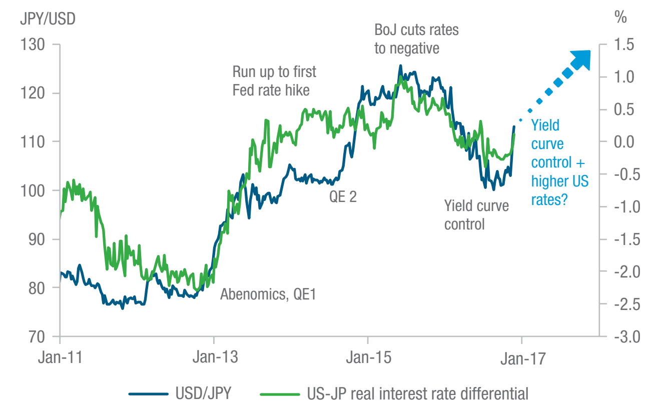
EU-US 10-year real interest rate differential and EUR/USD



Source: Bloomberg, Standard Chartered

Figure 3: Japan's policy of capping 10-year yields means US rates are now key to dragging USD/JPY higher

US-Japan 10-year real interest rate differential and USD/JPY



Source: Bloomberg, Standard Chartered

POUND STERLING

Short term | Medium term

GBP: Not out of the woods yet

The GBP plummeted following the Brexit vote in 2016. Despite this, we retain our medium term negative outlook on the GBP for three main reasons.

First, the UK has the highest current account deficit among major developed economies which has historically not adjusted quickly to a weaker GBP. Second, capital outflows could accelerate as bond holders capitulate amid narrowing real yield differentials with the US. Third, uncertainty regarding the UK's future relationship with the EU will continue to hurt investor sentiment and reduce appetite for UK assets. The main risk to this view is an increasing willingness by UK authorities to retain the existing economic engagement with the EU. Another risk is that should the Supreme Court require a parliamentary debate, UK lawmakers could agree to remain within the European Union, though the likelihood of this is low, in our opinion.

AUSTRALIAN DOLLAR

Short term | Medium term

NEW ZEALAND DOLLAR

Short term | Medium term

CANADIAN DOLLAR

Short term | Medium term

AUD, NZD and CAD: Riding on the back of reflation

We expect the AUD to extend its strength into 2017 against the backdrop of higher inflation scenarios (cumulatively 55% probability, see page 11), which is positive for commodity-linked currencies.

In our view, there are two main drivers of the AUD: commodity prices and central bank policy. We believe iron-ore prices bottomed in 2016 and could remain stable or gradually edge higher amid continued stimulus by China authorities. In addition, the rate cutting cycle has likely ended, in our opinion, as global inflation spills over into Australia and the Reserve Bank of Australia (RBA) grows less concerned about currency strength. A move towards a deflationary scenario would be the main risk to our constructive AUD outlook.

Similar to the AUD, two key factors shape the outlook for the NZD and the CAD: key commodity prices and interest rate differentials with the US. An improved outlook for key commodities (Dairy for NZD and Oil for CAD) is likely to be supportive for the currencies. Moreover, we do not expect further monetary easing by either the Reserve Bank of New Zealand (RBNZ) or the Bank of Canada (BoC) which is likely to limit the widening of interest rate differentials in favour of the USD. Global deflationary threats are the main risk to our view.

Emerging Market Currencies

We expect Emerging Market (EM) currencies to remain under pressure as we head into 2017. This is likely to be due to rising US rates and a stronger USD. However, a reflationary environment driven by higher commodity prices and a better growth outlook in Developed Markets is likely to be supportive for EM currencies. For this reason, we do not believe further declines in EM currencies are likely to be as broad-based as in the 2014-2015 period (see Figure 6 on page 63). We also see room for differentiation in the EM currency space.

Figure 4: Higher commodity prices amid growth stability in China likely to drive the AUD/USD higher

China iron-ore prices and AUD/USD

Source: Bloomberg, Standard Chartered

CHINESE YUAN

Medium Term

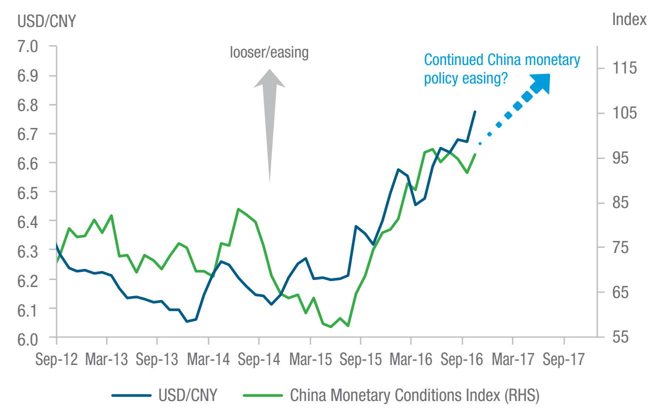
CNY: Further downside expected

We maintain our bearish outlook for the CNY heading into 2017.

First, the impact from higher US rates and broad USD strength is negative. Higher US rates are likely to result in continued corporate deleveraging or capital outflow from China which could pressure the currency. Second, we believe China is likely to maintain a broadly accommodative stance, which implies allowing the CNY basket to weaken in-line with market expectations. The main upside risk to our outlook is a shift in the policy easing stance in China or a broadly weaker USD.

Figure 5: Continued monetary easing in China to drive USD/CNY higher

China monetary conditions index and USD/CNY



Source: Bloomberg, Standard Chartered

SOUTH KOREAN WON

Medium Term

KRW: Driven by external factors

We expect the KRW to weaken on the back of a stronger USD going into 2017, but it could stabilise once most bullish USD factors such as higher US rates are priced in.

In the immediate term, concerns regarding the potentially negative impact of protectionist US trade policies, the Bank of Korea's (BoK) accommodative monetary bias and our expectation of a weaker JPY are negative for the KRW. Further into the year, we could see more stability once most USD supportive factors above are priced-in and sentiment towards EM improves. Key upside risks to our view include a weaker USD or a stronger JPY and a shift in domestic monetary policy to a less accommodative stance which could result in KRW gains.

SINGAPORE DOLLAR

Medium Term

SGD: More downside ahead

Similar to the region as a whole, we believe the SGD is likely to weaken as the Fed hikes interest rates. Beyond this, we believe a weak domestic growth outlook, weakening property prices coupled with persistently low inflation may increase expectations of further MAS policy easing. This poses further downside risk to the SGD.

MALAYSIAN RINGGIT

Medium term

THAI BAHT

Medium term

PHILIPPINE PESO

Medium term

MYR, THB and PHP: We remain cautious

We expect MYR weakness to extend heading into 2017. The MYR is one of the most sensitive regional currencies to USD strength, trade flows and commodity prices. Thus, the MYR is vulnerable in case of a regional currency sell-off due to a small current account surplus, the high foreign ownership of the local bond market and low FX reserve levels. A rise in commodity prices over the medium term could, however, limit MYR downside.

We expect the THB to weaken against the USD along with regional currencies given the export-oriented nature of the economy and potential for capital outflows. However, Thailand's stronger balance of payments position relative to Malaysia may allow the THB to be more resilient than the MYR.

The PHP is less exposed to external factors. However, it faces a deteriorating trade and foreign investment outlook in the immediate term. The domestic growth outlook, though, is likely to be supportive.

INDIAN RUPEE — Medium term

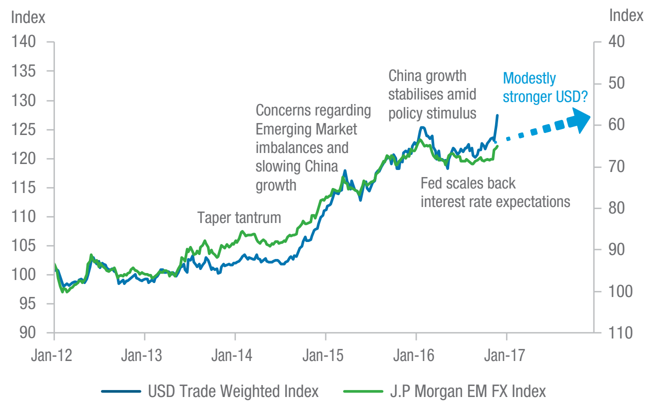
INDONESIAN RUPIAH — Medium term

IDR and INR: Domestically oriented with high carry

The INR and IDR are expected to remain more resilient than regional peers for three main reasons. First, both countries offer high interest rates, which could cushion downside should regional currencies weaken. Second, both currencies are less exposed to global trade as it accounts for a smaller percentage of GDP. Third, both countries have reasonable domestic reform and growth outlooks which could increase the attractiveness of their assets.

Figure 6: Emerging Market Currencies closely follow the broad USD

USD trade weighted index and J.P Morgan EM FX index



Source: Bloomberg, Standard Chartered

BRAZILIAN REAL — Medium term

RUSSIAN RUBLE — Medium term

BRL and RUB: Commodity exposure positive

We expect the BRL and RUB to remain more resilient relative to EM peers for three reasons. First, both the BRL and RUB are significantly exposed to commodities and we see a more positive outlook for prices in 2017. Second, a significant degree of political and economic risk scenarios may have already been priced-in. Third, both offer very attractive yields which should offer some downside protection.

KEY INVESTMENT THEMES AT A GLANCE

1 EUR/USD to fall

2 AUD/USD to rise

3 USD/CNY to rise

4 We expect an equally weighted basket of IDR, INR, RUB and BRL to outperform the broad EM currency index

Short term = under 3 months
Medium term = 3-12 months

SOUTH AFRICAN RAND — Medium Term

TURKISH LIRA — Medium Term

ZAR and TRY: Downside risks persist

We are cautious on the ZAR and TRY for two common reasons. First, both have a weaker balance of payments profile compared to other major peers which makes them more susceptible to USD gains. Second, political risks (in case of South Africa) and security risks (in case of Turkey) are likely to further dampen investor appetite.

COMMODITIES AT A GLANCE

[Tariq Ali, CFA | Manpreet Gill]

KEY THEMES

We expect commodities to moderately extend their upside into 2017, amid an improving outlook for inflation and the global capital expenditure cycle.

Oil prices likely to rise further. The improving demand-supply fundamentals suggest oil prices are likely to move higher in 2017, but remain capped around USD60-65/bbl.

Gold likely to remain range-bound. Very limited gold exposure remains justified as a hedge against an inflationary downside scenario.

Modest upside in industrial metals to continue into 2017 on the back of a reflationary environment, though significant demand-supply imbalances do not provide conviction for a strong bullish view.

KEY DRIVERS

Commodity	View	Inventory	Production	Demand	Real Interest Rates	USD	Risk Sentiment	Comments
Oil	◆	Not supportive	Supportive	Supportive	n/a	Neutral	Supportive	Inventories high; demand-supply gap to shrink
Gold	◆	Neutral	Neutral	Neutral	Neutral	Neutral	Not supportive	US rate increases expected to be in-line with inflation
Metals	◆	Neutral	Neutral	Supportive	n/a	Neutral	Supportive	China demand a support; market still oversupplied

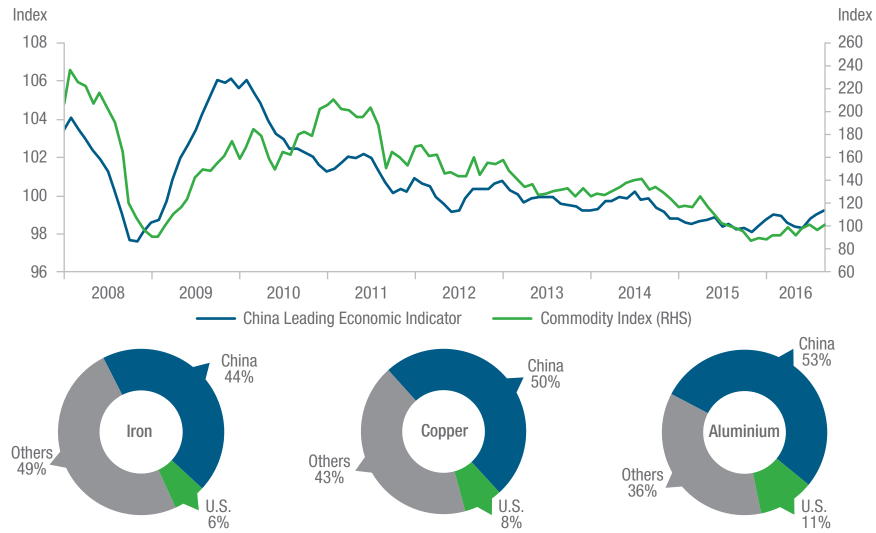
Source: Bloomberg, Standard Chartered
Legend: ◆ Neutral | ● Not supportive | ● Neutral | ● Supportive

KEY CHART

China is among the largest consumers of most major commodities, hence stability there remains critical for continued upside in commodities

Figure 1: Pick-up in China growth improves outlook for commodities

China leading economic indicator and Bloomberg commodity industrial metals sub-index, China's consumption share of key industrial metals (below)



Source: Bloomberg, Standard Chartered

REFLATION AND CHINA STABILITY

Overall commodity outlook

After posting a decline for several years, commodity prices rose in 2016 as demand-supply imbalances grew less severe and as China implemented policy stimulus (both fiscal and monetary). In 2017, we are more constructive on commodities than in 2016.

We highlight the following factors which support a moderately bullish commodities outlook. First, our expectations of higher inflation scenarios (cumulatively 55% probability, see page 11) are constructive for commodities as these usually coincide with a pick-up in demand as companies increase capital expenditure. Second, demand-supply imbalances will likely further narrow, although this is likely to be more pronounced in the case of oil. Third, China is likely to maintain stability through continued monetary and fiscal expansion.

Key risks to our outlook include resurgence of deflationary risks, OPEC producers failing to effectively implement agreed production cuts and a significant deterioration in China's growth outlook.

Energy: Tightening markets...finally

Oil prices recovered in Q1 2016, after falling through most of 2014-2015. Since then, the move higher in oil has been gradual and subject to pullbacks. In 2017, we expect factors favouring a higher oil price to take hold, although we still do not expect prices to sustain above USD60-65/bbl.

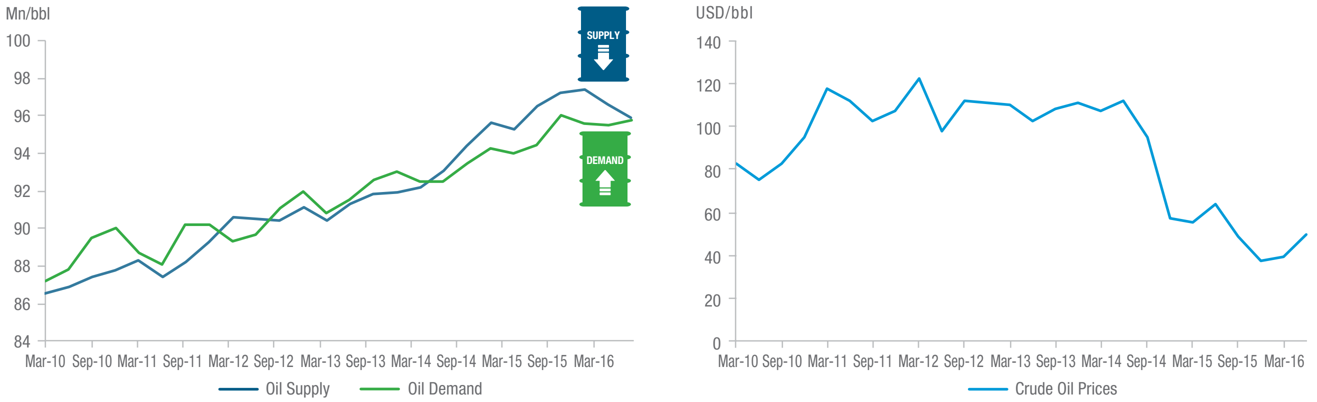
Slower supply growth remains the main driver behind our expectation of higher prices next year. The deal among OPEC members is significant. Key OPEC players and Russia also reached a consensus to cut production. Meanwhile, US production growth continues to decline consistently, while inventory build-up stabilised in 2016. Against this backdrop, we see demand-supply gap moving into deficit by mid next year, which may accelerate price gains into the second half of 2017.

Nonetheless, for three reasons, we do not believe the adjustment higher in oil prices is likely to be smooth. First, there are considerable headwinds to a smooth implementation of production curtailment among OPEC members and, hence, this will be a key source of volatility for oil markets. Second, we believe prices in excess of USD60-65/bbl are likely to bring in an additional layer of supply from higher cost producers (including US shale) notably limiting price gains beyond this. Third, modest USD strength could present an additional headwind, though the effect is likely to be modest.

We see the demand side as being supportive for oil prices into 2017. Most of the new demand for oil is coming from large Asian economies including China, India and Indonesia where we expect growth to remain resilient in 2017. In addition to this, US growth is also likely to pick up pace in 2017, which would be incrementally supportive to demand.

Figure 2: Tightening of supply-demand gap and eventual supply deficit to put upward pressure on prices

IEA total oil supply and demand and Brent oil prices (right)



Source: Bloomberg, Standard Chartered

Supply-demand imbalances improving much faster for oil than they are for industrial metals.

Industrial metals: Focus on China, not the US

Industrial metals rebounded strongly in 2016. A stablisation in China growth and pick-up in the property sector following government stimulus measures were supportive for base metals. From here on, we expect a modest uptrend in base metals, but do not expect a strong rally.

In our view, base metals are likely to continue to find support from China's continued policy easing and measures to support domestic demand. Despite recent optimism, we do not believe even an ambitious US fiscal stimulus can have a very meaningful impact on the demand for industrial metals. The US accounts for under 10% of total demand while China, which accounts for 50% remains the largest source of demand for industrial metals.

We believe two variables are likely to limit price gains in industrial metals. First, costs for large producers are still considerably below market prices, which give them room to increase production. In the case of iron-ore, production costs for large Australian producers are still roughly 50% below current prices, mostly on account of achieving more efficient production. Second, inventories for a number of key metals remain elevated, with demand unlikely to be strong enough to force a significant drawdown. For example, copper faces significant excess supply in 2017 and markets are likely to remain in surplus through the year.

Upside risks to our view include a stronger than expected growth rebound in China, acceleration of China government spending plans and faster producer cutbacks. Downside risks stems from a resumption of deflationary pressures or a significant deterioration of China's growth outlook.

Gold: Glittering less than before

Gold prices have edged lower over 2012-2015 but rebounded in 2016 as the Fed scaled back interest rate hike expectations. We turned positive on gold in mid-2016 as we expected a tepid Fed rate hike scenario, limited headwind from the USD and persistent risks in some areas of global growth. Looking into 2017, we believe positive and negative factors have become more balanced.

We believe three factors are likely to shape the outlook for gold price in 2017:

- interest rates net-of-inflation,
- the USD outlook, and
- safe-haven demand amid bouts of political and financial market stress.

We believe US interest rates will rise in-line with inflation expectations in 2017, which is neutral for gold. Our expectation of a stronger USD is likely to be a headwind for gold. Finally, we see a number of possible avenues for political tensions in 2017 which would increase safe-haven demand for gold, including possible trade related tensions and Euro area politics. Given the balance of risks, we maintain a neutral outlook for gold heading into 2017 and see opportunities in being tactical through the year.

Downside risks to gold include a much faster rise in interest rates relative to inflation, driving TIPS yields higher and a decline political stress. Upside risks to gold include a significant scale back in interest rates relative to inflation expectations, a broadly weaker USD and significant rise in political and banking sector stress.

Figure 3: Gold prices have followed 10-years TIPS yields inversely (a proxy for real interest rate expectations) very closely in recent times

US-10 year TIPS yield, gold price spot

US 10-year yield and 10-year inflation expectations

Source: Bloomberg, Standard Chartered

KEY INVESTMENT THEMES AT A GLANCE

Brent crude oil price to be higher by end 2017

ALTERNATIVE STRATEGIES
AT A GLANCE

[Manpreet Gill]

KEY THEMES

We believe Alternative Strategies continue to offer both a source of diversification and appropriate asset class substitution. This argues a diversified allocation to a basket of sub-strategies remains attractive in today's investment environment across a range of scenarios. See page 36 for more details on building a diversified allocation to Alternative Strategies.

We continue to believe global macro strategies offer value for their insurance-like characteristics. While total returns in 2016 YTD have been disappointing, its behaviour remains consistent with an insurance-like asset, which we believe remains relevant in 2017.

Equity hedge strategies represent attractive substitutes for long-only exposure during volatile equity markets which remains valuable given significant market pullbacks remain a risk late in the economic cycle.

KEY DRIVERS

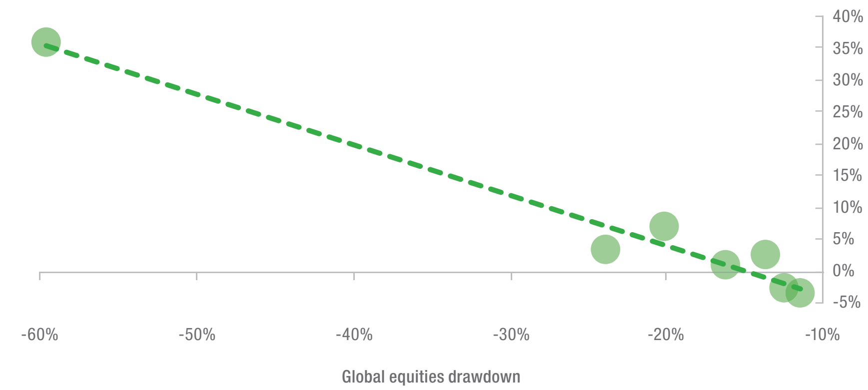
Asset Allocation	View	Asset class substitute?	Source of diversification?	Comments
Alternative Strategies	◆	🟢	🟢	A key source of diversification
Equity hedge	◆	🟢	🔴	Alternative to long-only equities
Relative value: credit	◆	🟢	🔴	Defaults are a risk
Relative value: ILS	▼	🟢	🔴	Average disaster-loss could rise
Relative value: others	◆	🟢	🔴	Liquidity challenging
Event-driven	◆	🟢	🔴	Deal spreads attractive for M&A
Global macro: commodities	◆	🔴	🟢	Rising oil prices a support
Global macro: others	▲	🔴	🟢	Offers insurance value

Source: Bloomberg, Standard Chartered
Legend: ▲ Most preferred | ▼ Least preferred | ◆ Neutral | 🔴 Not supportive | 🟡 Neutral | 🟢 Supportive

KEY CHART

CTA Strategy returns (a type of global macro strategy) are inversely correlated to equity market returns during >10% equity corrections

Figure 1: Trend-following (CTA) strategy returns vs. equity market corrections
Jan-2005 to date (dotted line shows line of best fit)



Source: Bloomberg, Standard Chartered

LOOKING FOR INSURANCE-LIKE ASSETS

Overview

Alternative Strategies had a mixed year in 2016 as excessively policy-driven markets, a sharp equity market drawdown in Q1 and bonds' outperformance relative to equities over H1 this year worked against many alternative strategies. While the asset class eked out a positive return for the year, much of this came from event-driven strategies.

As a source of insurance, thus, macro strategies did extract a premium, though this is not surprising as equities delivered positive returns.

Diversified exposure and asset class substitutes

This mixed performance notwithstanding, we continue to believe a basket of Alternative Strategies remains attractive under a range of macroeconomic scenarios. See page 36 for more details on constructing a diversified Alternative Strategies allocation and page 11 for more details on our scenarios.

Many of the sub-strategies act as attractive substitutes for long-only exposure (eg. equity hedge as an alternative to equities) while others offer diversification value (eg. macro strategies, which have a relative low correlation with equities).

Within this framework, we believe equity hedge strategies remain attractive substitutes for long-only equities exposure. This was on display in early 2016, for example, when they outperformed equities during the market pullback. Select event-driven strategies should also benefit from continued mergers and acquisitions activity, particularly if repatriation of earnings by US companies accelerates.

Prefer global macro

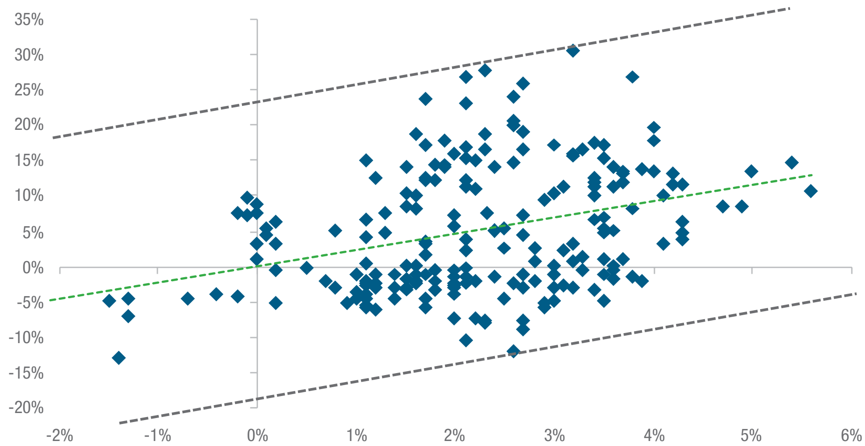
On the diversifiers side, we believe macro strategies do a better job than others of offering 'insurance-like' characteristics. Macro strategies have a reasonable track record as an insurance-like asset; as the chart on page 69 illustrates, in most equity market corrections (i.e. a global equities drawdown of 10% or more), CTA strategies (a subset of global macro strategies) have, in most cases, helped cushion against this pullback. A long-term negative correlation with bonds (see page 37) means this insurance-like characteristic also holds against the risk of rising bond yields over time.

This characteristic may be helpful especially when we start considering our range of scenarios. A reflationary scenario may moderate or reduce the frequency of significant equity market pullbacks, but, as we have learnt both through the equity market corrections in 2016 and the history of late-cycle behaviour, significant market pullbacks are still likely.

A move to an uncontrolled inflationary scenario (see macro section for details), which would likely hurt both equity and bond markets, would mean the diversification offered by macro strategies is even more useful. The chart on the left illustrates that macro strategies have a positive relationship with inflation, a characteristic that boosts the strategy's appeal as a source of insurance especially if US inflation surprises to the upside. The negative correlation with bonds over time is also likely to help.

Figure 2: Macro strategies' returns rise as US inflation rises, albeit within a relatively wide range

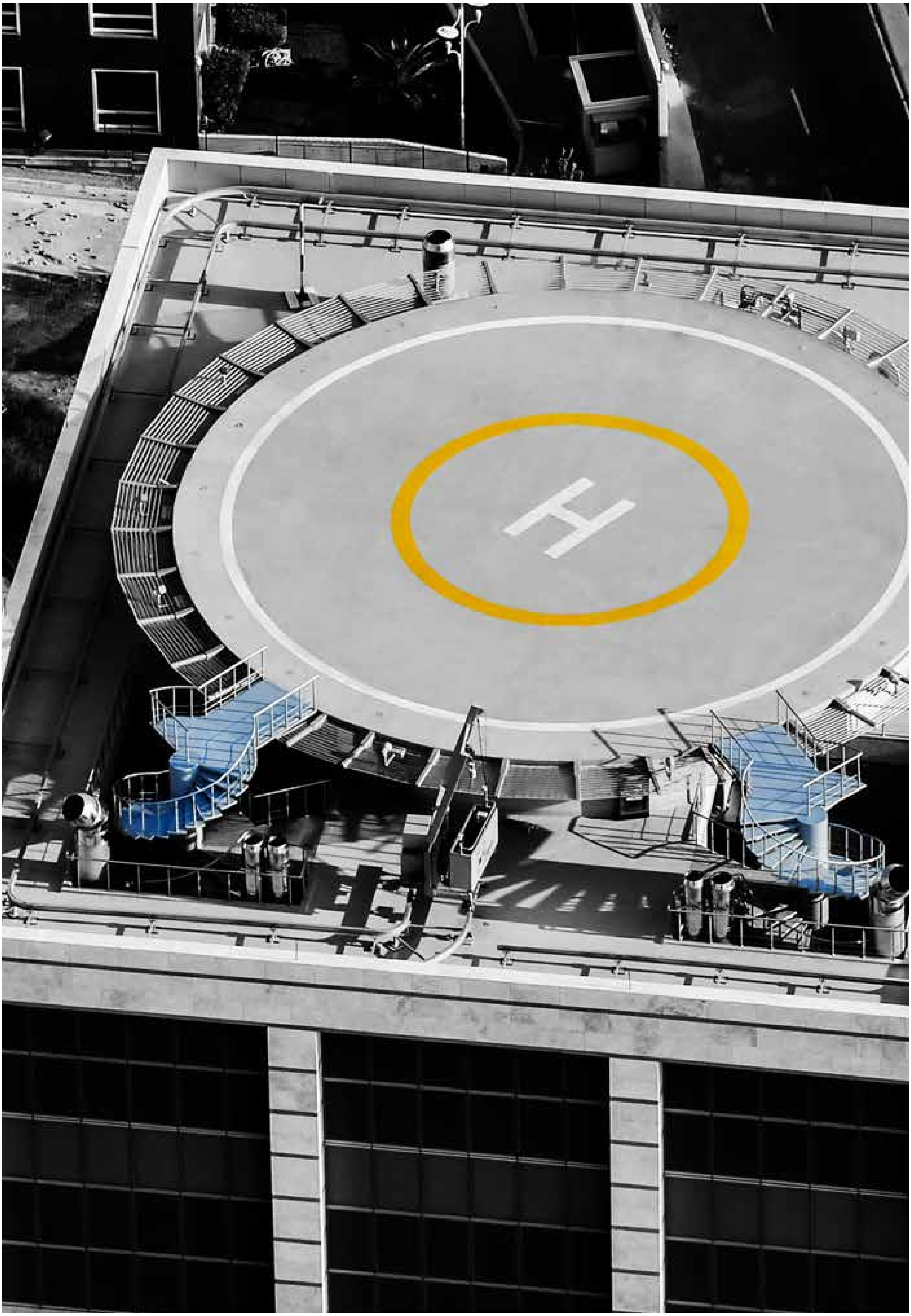
HFRX Macro Index returns (y/y) vs. US CPI inflation (y/y), monthly data. Dotted green line is linear line of best fit while dotted grey line shows range



Source: Bloomberg, Standard Chartered

KEY INVESTMENT THEMES AT A GLANCE

Our alternative strategies allocation to deliver positive absolute returns in 2017 (see page 36)



ASSET ALLOCATION SUMMARY

		View vs. SAA	Conservative	Moderate	Moderately Aggressive	Aggressive
Cash		Underweight	24	4	3	2
Fixed Income		Underweight	38	37	18	4
Equity		Overweight	23	39	60	86
Commodities		Neutral	5	10	10	5
Alternative Strategies		Neutral	10	10	9	3
Asset Class	**Region**					
Cash & Cash Equivalents	USD Cash	Underweight	24	4	3	2
Developed Market (DM) Investment Grade (IG) Bonds	DM Government Bonds*	Underweight	20	12	0	0
	DM IG Corporate Bonds*	Neutral	6	4	2	0
Developed Market High Yield (HY) Bonds	DM HY Corporate Bonds	Overweight	2	7	6	2
Emerging Market Bonds	EM USD Sovereign Bonds	Neutral	4	5	3	0
	EM Local Ccy Sovereign Bonds	Neutral	2	4	3	0
	Asia Corporate USD Bonds	Neutral	4	5	4	2
Developed Market Equity	North America	Overweight	8	13	20	28
	Europe ex-UK*	Neutral	4	7	9	15
	UK	Underweight	0	0	2	3
	Japan*	Overweight	2	4	6	8
Emerging Market Equity	Asia ex-Japan	Neutral	7	13	19	26
	Non-Asia EM	Neutral	2	2	4	6
Commodities	Commodities	Neutral	5	10	10	5
Alternative Strategies		Neutral	10	10	9	3

*FX-hedged exposure. All figures in %. For illustrative purpose only. Please refer to the Important information section at the end of this document for more details.
Source: Standard Chartered

2017 KEY EVENTS

JAN

19 ECB Policy Decision
20 US Presidential Inauguration Day
31 BOJ Policy Decision

FEB

02 FOMC Policy Decision

MAR

09 ECB Policy Decision
15 Netherlands Parliamentary Elections
16 FOMC Policy Decision
16 BOJ Policy Decision

APR

01 India's Possible Rollout of Nationwide Goods and Services Tax (GST)
23-30 France's Presidential Elections (two rounds)
27 BOJ/ECB Policy Decision

MAY

01-07 France's Presidential Elections (two rounds)
04 FOMC Policy Decision
27-08 India's Uttar Pradesh State Election

JUN

X France's Legislative Elections
08 ECB Policy Decision
15 FOMC Policy Decision
16 BOJ Policy Decision

JUL

20 BOJ Policy Decision
20 ECB Policy Decision
27 FOMC Policy Decision

AUG

N.A.

SEP

X Germany's General Elections
07 ECB Policy Decision
21 FOMC Policy Decision
21 BOJ Policy Decision

OCT

X China's 19th National Party Congress
26 ECB Policy Decision
31 BOJ Policy Decision

NOV

02 FOMC Policy Decision

DEC

14 ECB meeting
14 FOMC Policy Decision
21 BOJ Policy Decision

Legend: **X** – Date not confirmed | **ECB** – European Central Bank | **FOMC** – US Federal Open Market Committee | **BOJ** – Bank of Japan

2016 IN REVIEW

[Manpreet Gill]

Performance of key themes

One key framework we used to navigate the investment environment in 2016 was to consider a range of possible scenarios and what they implied for investment decisions. At a macro level, our scenarios proved accurate, with our core 'muddle-through' scenario largely playing out as the US economic expansion extended for yet another year.

However, there were two disappointments. First, the political shift towards greater populism was not on our radar screens. Second was the speed at which fiscal policy took centre stage; while this has not yet actually resulted in a rise in government spending, markets have moved in response to the potential for greater future spending (eg. US Treasury yields are higher). While concerns of a potential US recession were very much on our radar at the start of the year, many economic and cycle indicators suggest this is now less of an imminent worry.

This mix of accuracy and disappointment fed through into the outcome of our asset allocation decisions. Relative to 2015, we were less successful in capturing opportunities for outperformance. With the benefit of hindsight, we may have been too conservative. Having said that, absolute returns of our tactical asset allocation decisions in 2016 were higher (at 7.4%, Outlook 2016 to date, moderate risk profile) than those in the prior year (-1.7%, Outlook 2015 to Outlook 2016, moderate risk profile) amid supportive market momentum and our successful upgrade to fixed income in May.

A — **Advanced economies at different stages of the economic cycle.** Equity bull market likely to extend; Euro area (FX-hedged) and Japan our most preferred markets.

D — **Deflationary pressures to abate in developed markets.** Gold to stabilize in Q1 and US high yield bonds expected to perform well.

A — **Asia and Emerging Markets still dependent on China.** China our preferred market in Asia. Non-Asia Emerging Markets may bottom in 2016.

P — **Policies of central banks to remain supportive of growth.** USD bonds likely to deliver modest, but positive, returns. Income investing remains valid. USD strength to become less broad-based.

T — **Transition to late cycle likely to lead to higher volatility.** Investors need to take into account drawdown risks. Increase allocation to bonds and alternative strategies.

A

Our view of an extended global equity bull market held up year-to-date (10.3% since Outlook 2016), but it was tested both at the start of 2016, with a greater-than-10% pullback, and briefly over the summer. We started the year Overweight Euro area equities (on a FX-hedged basis) and Japanese equities. However, we closed both during early-2016 volatility at a loss – too early, with the benefit of hindsight – but risk-management considerations were the primary driver at the time.

D

After averaging just 0.1% y/y in 2015, US CPI inflation accelerated in 2016 to a year-to-date average of 1.1%. However, the abatement of deflationary pressures was less pronounced in the Euro area and absent in Japan. Gold recorded significant gains in Q1 (16.1%) amid equity market volatility and falling real (net-of-inflation) yields in the US. US HY bonds, meanwhile, ended just over 8 consecutive months of declines in mid-February and recorded an Outlook-to-date gain of 16.6%.

A

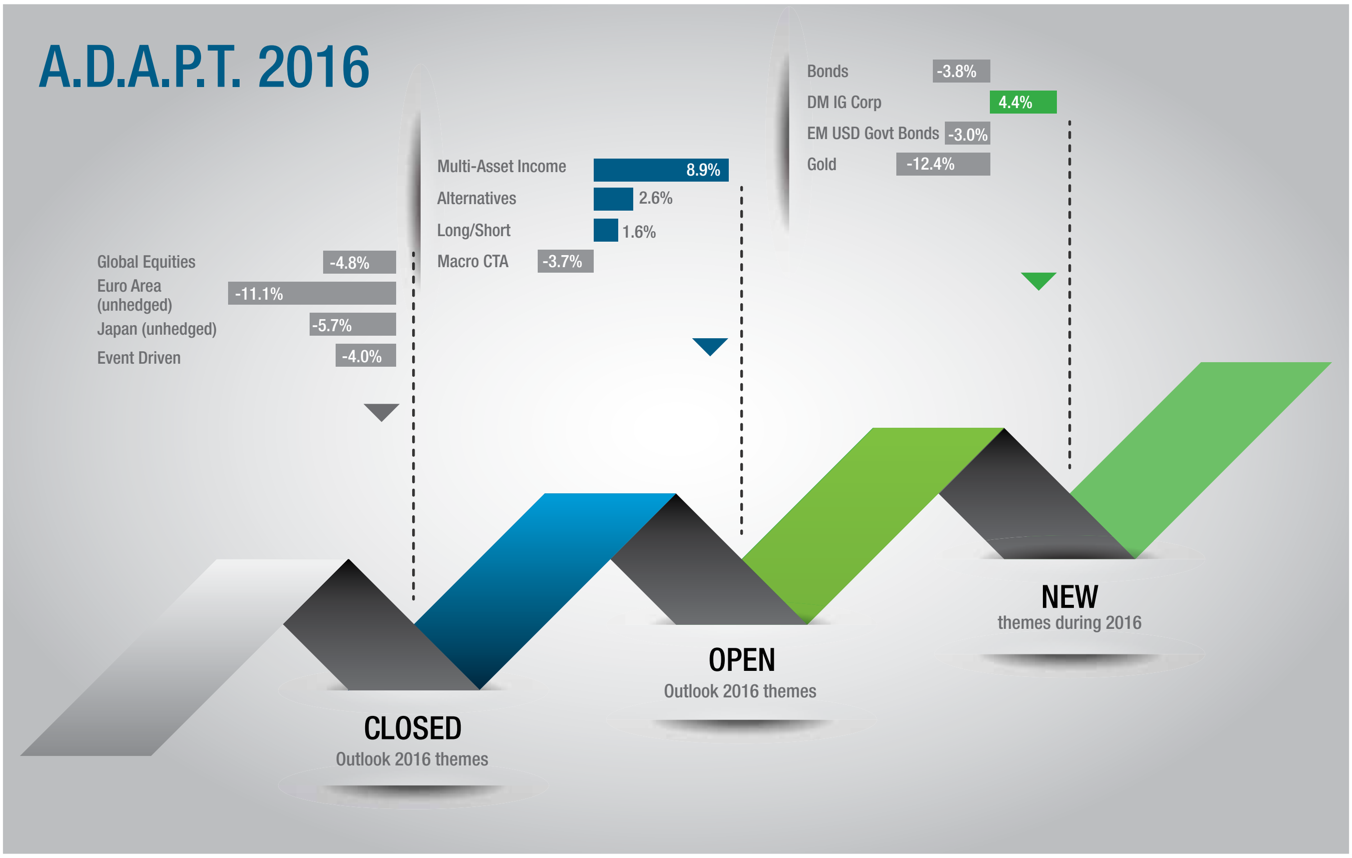
Emerging Market equities and hard currency bonds registered a sharp recovery through 2016 on stabilising Chinese growth and commodities, with EM equities outperforming Developed Market equities by 6.5% year-to-date. EM equities ex-Asia bottomed.

P

The Fed raised rates further only once in 2016, the Bank of Japan eased further and the ECB extended asset purchases. Most Emerging Market central banks either cut rates or left them unchanged. USD-denominated bonds recorded strong gains across the board in H1, though IG bonds partially pulled back in H2. Multi-asset income strategies gained 10% since Outlook 2016 at one point before pulling back over the past three months. The US Dollar index (DXY) remained range-bound, with upside pressure emerging after the US election.

T

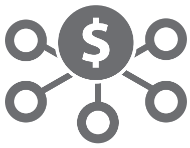
2016 was marked by two significant bouts of equity market volatility – first in Jan-Feb (resulting in a >10% equity correction) and second following Brexit (though this was smaller in magnitude). A third bout of volatility occurred in November following Trump’s surprise victory, but this was characterized by a pullback in bonds rather than equities. This resulted in bonds underperforming equities for the year.



Performance of three key A.D.A.P.T. themes

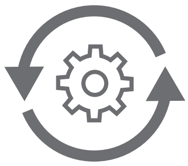
GLOBAL EQUITIES

-4.8%



MULTI-ASSET INCOME ALLOCATION

+8.9%



ALTERNATIVE STRATEGIES

+2.6%

Performance of our investment themes

Multi-asset income

Multi-asset income (MAI) strategies had a strong year and remains our top-performing investment theme in 2016 with 8.9% returns Outlook-to-date, though the strategy did suffer a pullback over the past three months.

Within MAI, top outperformers included US dividend yielding equities, US high yield bonds and convertible bonds. Key underperformers included European dividend yielding equities, US preferred equities and US inflation-protected bonds, though many of these underperformers still delivered positive absolute returns.

Bonds

Our view at the start of the year that bonds would outperform cash and commodities worked well (outperforming by 7.6% and 2.8% respectively). Our preferred bonds – IG corporate, US HY and EM USD bonds – also outperformed. Within government bonds, though, the outperformance of Japan Government Bonds surprised us (outperforming US Treasuries by 24% before we closed the view), as did the outperformance of local currency bonds in Latin American and Europe EM over Asia EM. Our favourable view on INR local currency bonds delivered absolute returns of 3.7% though a similar view on IDR bonds lost -2.9%.

Equities

Our preference for equities over bonds for a majority of H1 2016 worked against us (underperforming by -3.2%), though this is a view we closed far too early in the year given how equities rebounded thereafter. Within equities, Developed Markets outperformed Emerging (1.3%) and our expectation of underperformance in Japan (a reversal of the outperformance view we initially started the year with), UK, Singapore and Malaysia equities panned out along expected lines – see table on page 80 for details.

Our sector calls were less successful; US-listed technology underperformed by -0.6%, with most underperformance occurring post-US elections, and US banks underperforming by -7.8% until we closed the call in June 2016.

Commodities

Commodities had a stronger year than we expected (12.4% returns Outlook to date). The sharp rally in industrial metals (16.5% outperformance vs. broad commodities) surprised us. Our expected ranges for both oil (USD45-55) and gold (USD1250-1400) largely held, though gold did fall well below this range following Trump's election win. 'Consumption' commodities outperformed 'investment' commodities by 11.2%, as we expected.

Currencies

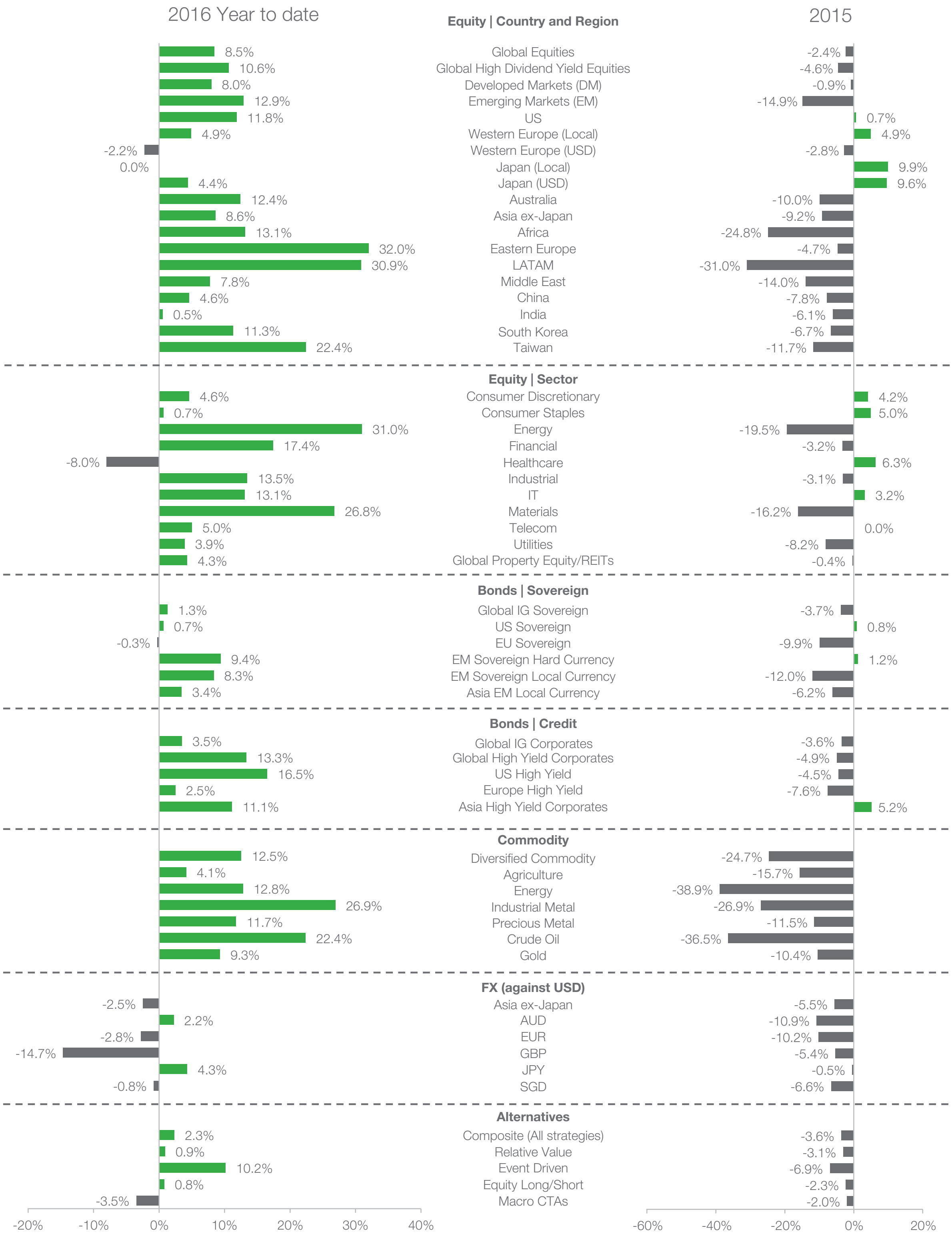
Our view the US Dollar would spend 2016 in a range largely worked out as expected, notwithstanding the short-lived break higher after the US election. We had success with our views on GBP, JPY and CHF, but not with our views on AUD, NZD and EUR – see table on pages 82-83 for details.

We had greater success with our views on Asian currencies, with the INR, IDR, MYR and THB outperforming regional currencies and SGD underperforming during our stated time periods. See table on pages 83-84 for details.

Alternative strategies

The asset class delivered positive returns Outlook 2016-to-date (2.6%), as expected. Equity long/short delivered positive returns over this period (1.6%). Global macro strategies disappointed with returns of -3.7% year-to-date, though it did help reduce drawdown risk during periods of volatility.

Figure 1: Market performance summary



Source: MSCI, JP Morgan, Barclays, Citigroup, Dow Jones, HFRX, FTSE, Bloomberg, Standard Chartered
*All performance shown in USD terms, unless otherwise stated.
The column '2016 Year to date' indicates performance from 31 December 2015 to 09 December 2016.
The column '2015' indicates performance from 31 December 2014, to 31 December 2015.

2016 PERFORMANCE SUMMARY

	Theme	Index Name#	Relative Benchmark##	Date Open	Date Closed	Absolute###	Relative####
	BONDS						
⬆	US 10-2 yield curve to flatten	US Treasury 10-2 yield spread		11 Dec 2015	21 Jun 2016	✔	n/a
⬆	Bonds to outperform Commodities (bonds FX-hedged)	Bond Blended Benchmark Index[1]	Bloomberg Commodity Index	11 Dec 2015	25 Mar 2016	✔	✔
⬆	Bonds to outperform Cash (bonds fx-hedged)	Bond Blended Benchmark Index[1]	JP Morgan Global Cash Index 3M	11 Dec 2015	09 Dec 2016	✔	✔
⬆	Prefer US Treasuries over German Bunds	Citi US GBI LCL	Citi Germany GBI USD	11 Dec 2015	25 Aug 2016	✔	✘
⬆	Prefer US Treasuries over Japanese Government Bonds	Citi US GBI LCL	Citi Japan GBI USD	11 Dec 2015	25 Aug 2016	✔	✘
⬆	Prefer DM IG Corporate Bonds over Sovereign Bonds	Citi World BIG Corp Index Hedged USD	Citi WorldBIG Govt/Govt Sponsored Index USD	11 Dec 2015	09 Dec 2016	✔	✔
⬆	Prefer US HY over Global Bonds	Barclays US Corporate High Yield TR Index Unhedged USD	Citi WorldBIG Index USD	11 Dec 2015	28 Apr 2016	✔	✔
⬆	Prefer US IG Corporate Credit over Global Bonds	Barclays US Agg Credit TR Value Unhedged USD	Citi WorldBIG Index USD	11 Dec 2015	09 Dec 2016	✔	✔
⬆	Prefer US IG Corporate Credit over EU IG Corporate Credit	Barclays US Agg Credit TR Value Unhedged USD	Barclays Euro Agg Corporate TR	27 Jun 2016	09 Dec 2016	✘	✔
⬆	Prefer EM USD over EM LCY	JPMorgan EMBI Global TR Index	JPMorgan GBI-EM Broad Diversified Unhedged USD	11 Dec 2015	09 Dec 2016	✔	✘
⬆	Prefer EM IG over EM USD Bonds	JPMorgan EMBI Global Diversified IG	JPMorgan EMBI Global TR	27 Jun 2016	09 Dec 2016	✘	✘
⬆	Prefer EM USD over DM USD Government Bonds	JPMorgan EMBI Global TR Index	Citi WorldBIG Govt/Govt Sponsored Index USD	27 Jun 2016	09 Dec 2016	✔	✔
⬆	Prefer Asia LCY over EMEA LCY	JPMorgan GBI-EM Diversified Asia USD Unhedged	JPMorgan GBI-EM Global Diversified EMEA Unhedged USD	11 Dec 2015	09 Dec 2016	✘	✘
⬆	Prefer Asia LCY over LATAM LCY	JPMorgan GBI-EM Diversified Asia USD Unhedged	JPMorgan GBI-EM Global Diversified LATAM Unhedged USD	11 Dec 2015	09 Dec 2016	✘	✘
⬆	Prefer Asian IG over Asian HY	JPMorgan JACI IG TR	JPMorgan JACI Non-IG Corporates TR	27 Jun 2016	09 Dec 2016	✘	✘
⬆	Prefer India Government Bonds LCY	CRISIL Composite Bond Fund Index (USD)		11 Dec 2015	21 Jun 2016	✔	n/a
⬆	Prefer Indonesia Government Bonds LCY	Iboxx ABF Indonesia TR Index (USD)		22 Jul 2016	09 Dec 2016	✘	n/a
	EQUITIES						
⬆	Prefer Equities over Bonds	MSCI All-Country World Daily TR Net USD	Citi WorldBIG Index USD	11 Dec 2015	21 Jun 2016	✔	✘
⬇	Underweight Global Equities	MSCI All-Country World Daily TR Net USD	Contribution to TAA[5]	27 Jun 2016	09 Dec 2016	✘	✘
⬆	Prefer Developed over Emerging Markets	MSCI World TR Net USD Index	MSCI Emerging Markets TR Net USD	27 Jun 2016	09 Dec 2016	✔	✔
⬆	Overweight US Equities	MSCI USA TR Net Index	MSCI All-Country World Daily TR Net USD	21 Jul 2016	22 Sep 2016	✔	✘

Theme	Index Name#	Relative Benchmark##	Date Open	Date Closed	Absolute###	Relative####
EQUITIES						
Overweight Euro (Hedged) Equities	MSCI EMU Index Hedged to USD	MSCI All-Country World Daily TR Net USD	11 Dec 2015	25 Feb 2016	✘	✔
Overweight Euro (Unhedged) Equities	MSCI EMU TR Net USD Index	MSCI All-Country World Daily TR Net USD	26 Feb 2016	21 Jun 2016	✔	✘
Underweight Euro (Unhedged) Equities	MSCI EMU TR Net USD Index	MSCI All-Country World Daily TR Net USD	22 Jul 2016	22 Sep 2016	✘	✘
Underweight UK Equities	MSCI UK TR Net USD Index	MSCI All-Country World Daily TR Net USD	11 Dec 2015	28 Apr 2016	✘	✔
Overweight Japan Equities	MSCI Japan Local TR Net USD Index	MSCI All-Country World Daily TR Net USD	11 Dec 2015	25 Mar 2016	✘	✘
Underweight Japan Equities	MSCI Japan Local TR Net USD Index	MSCI All-Country World Daily TR Net USD	23 Sep 2016	09 Dec 2016	✘	✔
Overweight Asia ex-Japan Equities	MSCI AC Asia ex-Japan TR Net Index	MSCI All-Country World Daily TR Net USD	26 Aug 2016	09 Dec 2016	✘	✘
Underweight Non-Asia EM Equities	MSCI EM ex Asia TR Net USD Index	MSCI All-Country World Daily TR Net USD	11 Dec 2015	21 Jul 2016	✘	✘
Prefer Defensives over Cyclicals	Composite of Global Defensive sectors[2]	Composite of Global Cyclical sectors[3]	27 Jun 2016	24 Nov 2016	✘	✘
Prefer Small/Mid caps over Large caps in Europe	MSCI Europe Mid and Small Cap TR Index (Blended)	MSCI Europe Large Cap TR Index	11 Dec 2015	09 Dec 2016	✔	✘
Overweight US-Listed Technology	US Listed Technology Sector Index (Price returns)[4]	MSCI United States Index (Price returns)	11 Dec 2015	09 Dec 2016	✔	✘
Overweight US Banks	MSCI USA Banks TR Index	MSCI United States TR Index	11 Dec 2015	28 Apr 2016	✘	✘
Overweight China Equities	MSCI China TR Net USD Index	MSCI AC Asia ex-Japan TR Net Index	11 Dec 2015	25 May 2016	✘	✘
Prefer MSCI China to China 'A' Shares	MSCI China TR Net USD Index	Shanghai Composite Index (USD)	26 Feb 2016	09 Dec 2016	✔	✔
Prefer India Equities within Emerging Markets	MSCI India TR Net USD Index	MSCI Emerging Markets TR Net USD	29 Apr 2016	20 Oct 2016	✔	✘
Underweight Singapore	MSCI Singapore TR Net USD Index	MSCI AC Asia ex-Japan TR Net Index	29 Apr 2016	09 Dec 2016	✔	✔
Overweight Taiwan	MSCI Taiwan TR Net USD Index	MSCI AC Asia ex-Japan TR Net Index	29 Apr 2016	21 Jun 2016	✔	✔
Overweight India	MSCI India TR Net USD Index	MSCI AC Asia ex-Japan TR Net Index	27 May 2016	09 Dec 2016	✔	✘
Overweight Korea	MSCI Korea TR Net USD Index	MSCI AC Asia ex-Japan TR Net Index	27 May 2016	09 Dec 2016	✔	✔
Underweight Hong Kong	MSCI Hong Kong TR Net USD Index	MSCI AC Asia ex-Japan TR Net Index	27 May 2016	22 Sep 2016	✘	✘
Overweight Indonesia	MSCI Indonesia TR Net USD Index	MSCI AC Asia ex-Japan TR Net Index	23 Sep 2016	09 Dec 2016	✘	✘
Underweight Malaysia	MSCI Malaysia TR Net USD Index	MSCI AC Asia ex-Japan TR Net Index	23 Sep 2016	09 Dec 2016	✔	✔

	Theme	Index Name[#]	Relative Benchmark[##]	Date Open	Date Closed	Absolute[###]	Relative[####]
	COMMODITIES						
⬇	Underweight Commodities	Bloomberg Commodity TR Index	Contribution to TAA[5]	11 Dec 2015	25 Mar 2016	✘	✘
⬇	Underweight Commodities	Bloomberg Commodity ex-Agriculture & Livestock TR Index	Contribution to TAA[5]	27 May 2016	21 Jul 2016	✘	✘
⇄	Average quarterly crude prices to not exceed $65/bbl	Brent Crude Spot		11 Dec 2015	09 Dec 2016	✔	n/a
⇄	Crude to bottom out within USD 25-30 in the next 3-6 months	Brent Crude Spot		26 Feb 2016	26 Aug 2016	✘	n/a
⇄	Crude to trade within USD45-55 in the next 3 months	Brent Crude Spot		27 Jun 2016	25 Jul 2016	✘	n/a
⇄	Crude to trade within USD45-55 by year end	Brent Crude Spot		28 Mar 2016	25 Jul 2016	✘	n/a
⇄	Crude likely to be capped at USD60-65/bbl in 2016	Brent Crude Spot		27 Jun 2016	09 Dec 2016	✔	n/a
⇄	Gold to stay within $1,000-1,200 in 2016	Gold spot		11 Dec 2015	11 Feb 2016	✘	n/a
⇄	Gold to stay within $1,150-1,250 in the next 3 months	Gold spot		26 Feb 2016	03 Mar 2016	✘	n/a
⇄	Gold to stay within $1,250-1,400 in the next 3 months	Gold spot		22 Jul 2016	22 Oct 2016	✔	n/a
⇄	Gold to stay within $1,250-1,400 to year end	Gold spot		27 Jun 2016	11 Nov 2016	✘	n/a
⬇	Negative on Industrial Commodities	Bloomberg Industrial Metals Index	Bloomberg Commodity Index	11 Dec 2015	09 Dec 2016	✘	✘
⬆	Prefer (zinc/aluminium/nickel) to (iron-ore/copper)	Zinc/Aluminium/Nickel Blend Index[6]	Iron Ore/Copper Blend Index[7]	11 Dec 2015	09 Dec 2016	✔	✔
	ALTERNATIVE STRATEGIES						
⬆	Overweight Alternative Strategies	HFRX Global Hedge Fund Index	Contribution to TAA[5]	11 Dec 2015	08 Dec 2016	✔	✔
⬆	Overweight Equity Long/Short Strategies	HFRX Equity Hedge Index	HFRX Global Hedge Fund Index	11 Dec 2015	08 Dec 2016	✔	✘
⬆	Overweight Event-driven Strategies	HFRX Event Driven Index	HFRX Global Hedge Fund Index	11 Dec 2015	25 Feb 2016	✘	✘
⬆	Overweight Global Macro Strategies	HFRX Macro/CTA Index	HFRX Global Hedge Fund Index	11 Dec 2015	08 Dec 2016	✘	✘
⬇	Underweight Insurance-linked Strategies	Eurekahedge ILS Advisers Index[8]	HFRX Global Hedge Fund Index	26 Feb 2016	30 Nov 2016	✘	✘
	CURRENCIES						
⇄	USD to remain broadly stable over 12-month horizon (116-126 range)	USD Broad Trade Weighted Index		27 Jun 2016	14 Nov 2016	✘	n/a
⇄	GBP/USD to stay within 1.45-1.60	GBP/USD		11 Dec 2015	11 Jan 2016	✘	n/a
⬇	Bearish GBP/USD	GBP/USD		27 Jun 2016	09 Dec 2016	✔	n/a

Theme	Index Name#	Relative Benchmark##	Date Open	Date Closed	Absolute###	Relative####
CURRENCIES						
Bearish EUR/USD	EUR/USD		11 Dec 2015	28 Apr 2016	✘	n/a
EUR/USD to stay within 1.05-1.15 in the next 12 months	EUR/USD		29 Apr 2016	02 May 2016	✘	n/a
EUR/USD to stay within 1.10-1.15 in the next 3 months	EUR/USD		22 Jul 2016	14 Oct 2016	✘	n/a
EUR/USD to stay within 1.05-1.15 in the next 12 months	EUR/USD		21 Oct 2016	09 Dec 2016	✔	n/a
Bullish USD/CHF	USD/CHF		11 Dec 2015	09 Dec 2016	✔	n/a
USD/JPY to stay within 116-126 in Q1 2016	USD/JPY		11 Dec 2015	08 Feb 2016	✘	n/a
USD/JPY to stay within 110-115 in the next 3 months	USD/JPY		27 May 2016	01 Jun 2016	✘	n/a
Bullish USD/JPY	USD/JPY		27 Jun 2016	21 Jul 2016	✔	n/a
USD/CAD to stay within 1.28-1.40	USD/CAD		11 Dec 2015	06 Jan 2016	✘	n/a
Bearish AUD/USD	AUD/USD		11 Dec 2015	28 Apr 2016	✘	n/a
Bearish AUD/USD	AUD/USD		27 May 2016	22 Sep 2016	✘	n/a
Bullish AUD/USD	AUD/USD		21 Oct 2016	09 Dec 2016	✘	n/a
Bullish AUD/NZD	AUD/NZD		29 Apr 2016	09 Dec 2016	✘	n/a
Bearish NZD/USD	NZD/USD		11 Dec 2015	09 Dec 2016	✘	n/a
Bearish ADXY	Bloomberg JP Morgan Asia Dollar Index		27 May 2016	21 Jun 2016	✘	n/a
Bullish USD/CNY	USD/CNY		29 Apr 2016	09 Dec 2016	✔	n/a
CNY to underperform trade basket	China CFETS		26 Aug 2016	09 Dec 2016	✘	n/a
Prefer MYR relative to ADXY	MYR Currency	Bloomberg JP Morgan Asia Dollar Index	11 Dec 2015	28 Apr 2016	✔	✔
Prefer IDR relative to ADXY	IDR Currency	Bloomberg JP Morgan Asia Dollar Index	11 Dec 2015	09 Dec 2016	✔	✔
Prefer INR relative to ADXY	INR Currency	Bloomberg JP Morgan Asia Dollar Index	11 Dec 2015	25 Mar 2016	✔	✘
Prefer INR relative to ADXY	INR Currency	Bloomberg JP Morgan Asia Dollar Index	27 May 2016	09 Dec 2016	✘	✔
Prefer PHP relative to ADXY	PHP Currency	Bloomberg JP Morgan Asia Dollar Index	27 Jun 2016	22 Sep 2016	✘	✘
Prefer THB relative to ADXY	THB Currency	Bloomberg JP Morgan Asia Dollar Index	27 Jun 2016	21 Jul 2016	✔	✔
Bullish USD/SGD	USD/SGD		26 Feb 2016	21 Jun 2016	✘	n/a

	Theme	Index Name#	Relative Benchmark##	Date Open	Date Closed	Absolute###	Relative####
	CURRENCIES						
⬇	SGD to underperform ADXY	SGD Currency	Bloomberg JP Morgan Asia Dollar Index	23 Sep 2016	20 Oct 2016	✔	✔
⬇	Bearish SGD/MYR	SGD/MYR		11 Dec 2015	09 Dec 2016	✘	n/a
	MULTI-ASSET INCOME[9]						
⬆	Multi-asset Income			11 Dec 2015	09 Dec 2016	✔	n/a
⬆	- Fixed Income			11 Dec 2015	09 Dec 2016	✔	n/a
⬆	- Equity Income			11 Dec 2015	09 Dec 2016	✔	n/a
⬆	- Non-core Income			11 Dec 2015	09 Dec 2016	✔	n/a

Source: Bloomberg, Standard Chartered

Performance measured from 11 Dec 2015 (release date of our 2016 Outlook) to 9 Dec 2016 or when the view was closed. Total returns are used for equity performance measurement unless indicated.

Notes:

1 Bond Blended Benchmark is a composite of 50% Citi Non-MBS WorldBIG index USD Hedged, 25% JPM EMBI Global Diversified IG, 12.5% Barclays Global HY TR, 12.5% JPM EMBI Global Diversified HY

2 Defensive index is a market-cap weighted composite of Staples, Healthcare, Telcos, Utilities sectors

3 Cyclical index is a market-cap weighted composite of Discretionary, Technology, Materials, Industrials sectors

4 US Listed Technology sector is a composite of 83% MSCI USA Tech index and 17% Bloomberg China ADR Index

5 Relative performance is captured as a positive or negative contribution to our Tactical Asset Allocation (TAA)

6 Zinc/Aluminium/Nickel Blend Index is an equal weighted composite of Zinc, Aluminium and Nickel 3M LME Rolling Forwards

7 Iron Ore/Copper Blend Index is an equal weighted composite of Iron ore (62% Fe Qingdao China) price and Copper 3M LME Rolling Forwards

8 Underweight on insurance-linked strategies for the period 26 Feb – 9 Dec 2016. Calculation is based on monthly index data (as of 30 Nov 2016)

9 Please refer to page 24 for more information

Explanatory Notes:

✔ – Correct call; ✘ – Missed call; n/a – Not Applicable

– Market index used to measure performance

– Simple absolute returns of the Index

Legends:

⬆ Overweight – Expected to return more than the relative benchmark

⬇ Underweight – Expected to return less than the relative benchmark

Bullish/Favour/Conviction – Expected to deliver positive returns

Flattening – A narrowing spread between long maturity and short-maturity yields

Past performance is not an indication of future performance. There is no assurance, representation or prediction given as to any results or returns that would actually be achieved in a transaction based on any historical data.

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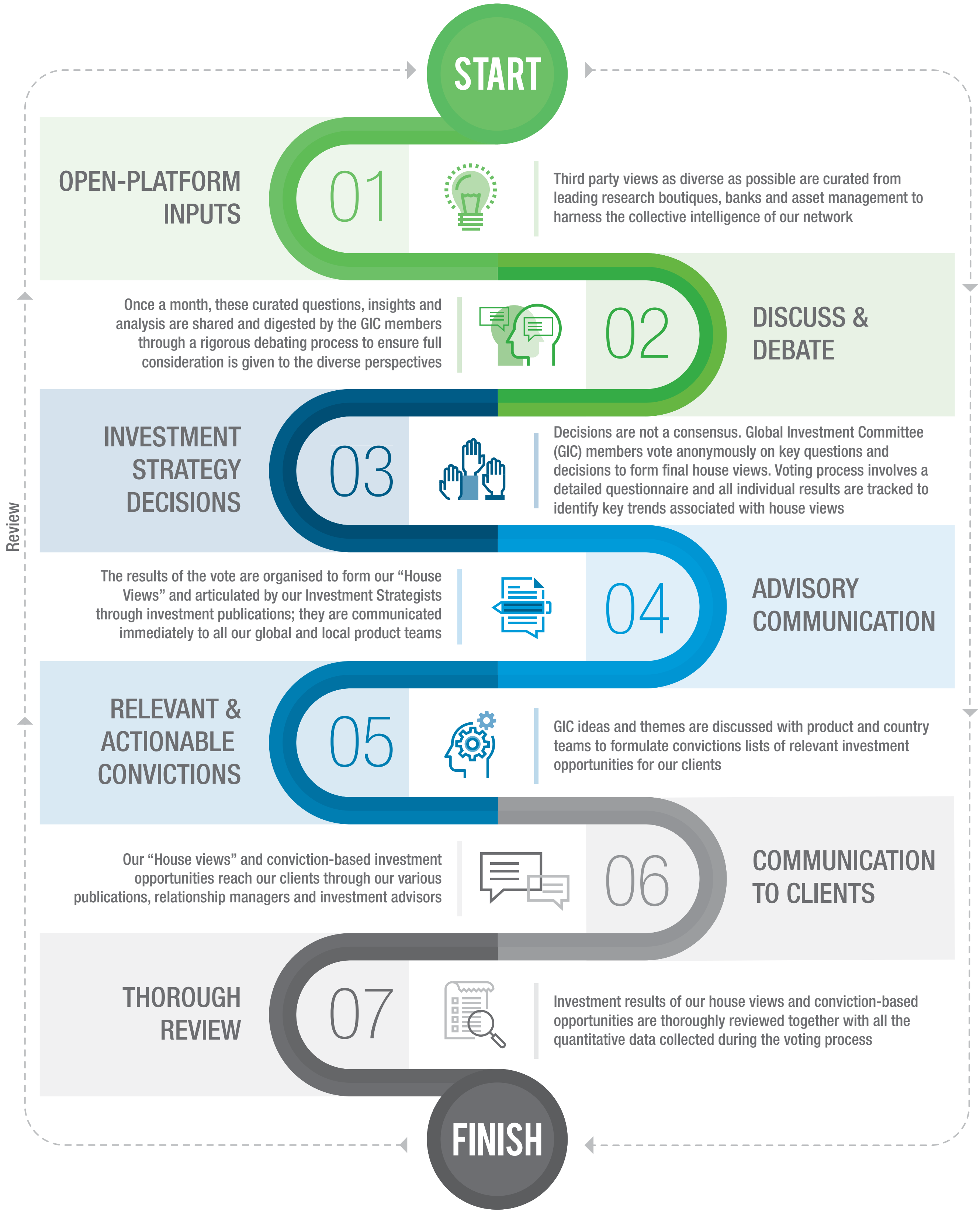
INVESTMENT VIEW GENERATION
OUR ROBUST PROCESS

We have a robust advisory process ensuring we deliver high-quality insights and solutions to our clients.



IMPORTANT INFORMATION

Explanatory Notes – 1. Figure 11 (page 34) show a multi-asset income asset allocation for a moderate risk profile only – different risk profiles may produce significantly different asset allocation results. Figures 11 (page 34) and the asset allocation diagram (page 72) are only examples, provided for general information only and they do not constitute investment advice, an offer, recommendation or solicitation. They do not take into account the specific investment objectives, needs or risk tolerances of a particular person or class of persons and they have not been prepared for any particular person or class of persons.

2. Contingent convertible securities are not intended to be sold and should not be sold to retail clients in the European Economic Area (EEA) (each as defined in the Policy Statement on the Restrictions on the Retail Distribution of Regulatory Capital Instruments (Feedback to CP14/23 and Final Rules) ("Policy Statement"), read together with the Product Intervention (Contingent Convertible Instruments and Mutual Society Shares) Instrument 2015 ("Instrument", and together with the Policy Statement, the "Permanent Marketing Restrictions"), which were published by the United Kingdom's Financial Conduct Authority in June 2015), other than in circumstances that do not give rise to a contravention of the Permanent Marketing Restrictions.

Here for good