After The Fall

SUMMARY

- **The S&P500 recorded a sharp 4.1% drop yesterday,** matched by similar weakness in the Dow and, to a lesser extent, high yield bonds. However, the 10-year US Treasury yield fell to 2.71%.
- **Our positive outlook on equities remains unchanged**. Economic and earnings fundamentals remain positive.
- **Indicators of short-term stress have moderated.** The 200DMA is key as historically, if the market rebounds from those levels, short term returns have been above-average.

BACKGROUND

- **US equities witnessed a sharp one-day drop**. The S&P500 closed 4.1% lower on Monday, with losses accelerating towards the end of the trading day. The fall meant the index fell through key support of 2685 we highlighted yesterday, but the index is now holding just above its 100 day moving average (DMA). US high yield bonds were lower, too, though by a much small magnitude.
- **10-year yields reversed to close lower at 2.71%**. Unlike last week, the equity drop was not accompanied by rising Treasury yields. Instead, 10-year bond yields fell intraday from above 2.88% to close at just below 2.71%.

WHAT DOES THIS MEAN FOR INVESTORS?

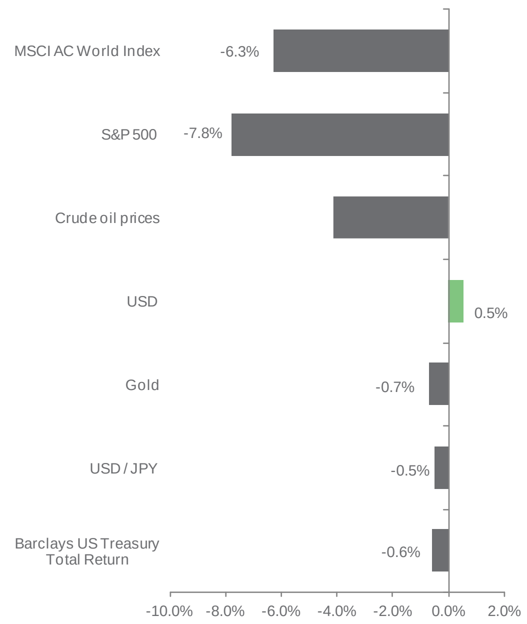
- **Spillover to Asian and Euro area equities could extend.** Both regions' equities fell yesterday, though this was likely only a catch-up to the move in the US. Weakness could extend this week.
- **Near-term technical indicators are moderating**. In the 19 January edition of the *Weekly Market View*, we had highlighted that select near-term technical indicators looked somewhat stretched. An update from today's level (see table) shows these have moderated, diminishing the likelihood of further, significant losses.
- **Little has changed on fundamentals, which remain very positive**. We believe it is important to keep in mind that little has changed on what remains a very positive fundamental picture. Earnings and economic growth fundamentals remain very strong while valuations are not yet at levels likely to constrain returns. Therefore, we maintain our positive view on equities, and look for incremental positive news to drive further gains.

WHAT TO WATCH OUT FOR

- **200DMA is key.** The 100DMA (0.6% below current levels) is the most immediate support level for the S&P500, but the 200DMA (4.3% below yesterday's close) is key; a rebound from here has historically signaled above-average positive returns in the short term, but a sustained drop below signals near-term weakness.
- **Policymaker comments.** The remainder of the week offers many opportunities for comments both from US policymakers (8 Fed Governor speeches are scheduled for this week) as well as central banks in Australia, the UK and India.

Weakness remains focused on equities since the most recent market peak on 26 January

Change in asset prices, 26-Jan-2018 to date



Source: Bloomberg, Standard Chartered

Indicators of stretched positioning have moderated

Short-term indicators for the S&P500

Indicators	Signal
Current level vs. 200DMA (S&P500)	🟡
Put/call ratio (S&P500)	🟡
Relative Strength Index (RSI) (S&P500)	🟢
VIX (S&P500)	🔴
MACD (momentum) weekly (S&P500)	🔴
Fund manager cash holding	🟡
Valuation backdrop (S&P500)	🔴

Source: Bloomberg, Standard Chartered

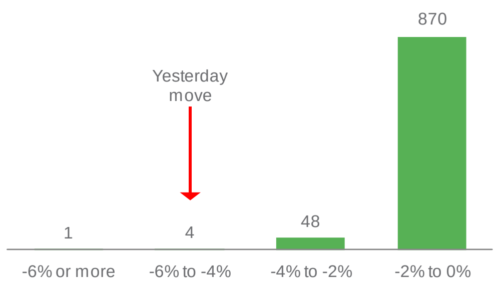
🔴 Higher risk of profit taking 🟢 Lower risk of profit taking

🟡 Moderate risk of profit taking

Source: Reuters, Standard Chartered

Large 1-day moves in S&P500 not unusual, but yesterday's move was larger than most

Distribution of one-day losses in S&P500 since 2010



Source: Bloomberg, Standard Chartered

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