Standard Chartered Private Bank

weekly **market view**

macro strategy | 8 March 2019

This reflects the views of the Wealth Management Group

Editorial

Beijing gives a boost to risk appetite

- **China's new fiscal stimulus adds to the tailwind from global monetary easing (ECB being the latest) and is positive for risk assets, especially in Asia ex-Japan and China.**
- **Equities:** The China A-shares' rally indicates strong underlying momentum, although the index appears overbought on some metrics. The next resistance is 3% above current levels.
- **Bonds:** Asia USD bonds likely to keep outperforming global bonds as demand outstrips supply. US Treasury yields may have bottomed as inflation expectations recover from January lows.
- **FX:** A decisive EUR/USD break below 1.1185 would raise the chance of a move towards 1.0865. We remain bearish on AUD.

What's new?

- **Beijing gives a boost to risk appetite.** China announced further tax cuts, enabled local governments to fund infrastructure and further opened up the economy to foreign investors. The budget deficit (after including local government bond issues) will rise to 5.0% in 2019, from 4.1% last year. The government also signalled more and cheaper credit for smaller companies. We expect further cuts in bank reserve requirements (following five cuts since the start of 2018) to enable banks to meet proposed lending targets and help stabilise economic growth (see page 3).
- **Tax cuts to lift China earnings.** We believe the larger-than-expected cuts in VAT rates and social security contributions (which follows last year's cuts in individual income taxes) will not only reduce costs for Chinese companies, but also likely boost consumption, lifting corporate earnings. Hence, we see scope for further upgrades to China's consensus earnings growth forecast, currently estimated at 12% for the next 12 months. China's stimulus, combined with a dovish turn in global monetary policies, support our bullish outlook for global equities, with a preference for Asia ex-Japan and China equities. They also support our preference for Asia USD and EM USD government bonds.
- **China A-share rally has legs.** The sharp rise in the Shanghai Composite index this year has echoes of the move in 2014-15. We believe market momentum remains very strong, implying further gains are likely even if some indicators suggest markets are overbought. Next resistance for the index is on the 200-week moving average (c.3,190), roughly 3% from current levels.
- **ECB extends easy policy guidance**. The ECB now expects to maintain its ultra-loose monetary policy till late 2019 – a further sign that global monetary policy has turned dovish. It also plans to resume interest-free loans (TLTRO) to banks from September for the first time since 2016. Although the ECB cut Euro area growth and inflation forecasts, we believe most of the slowdown has been priced in. In fact, Euro area growth appears to be stabilising, with an improving job market supporting the domestic services sector. Any breakthrough in the US-China trade talks and stabilisation in China's economy would be positive.

What we are watching

- a) US jobs report (8 March), b) UK parliament's vote on PM May's Brexit plan (12 March), c) US' decision on auto import tariffs, and d) if US Treasury yields break higher (see page 2).

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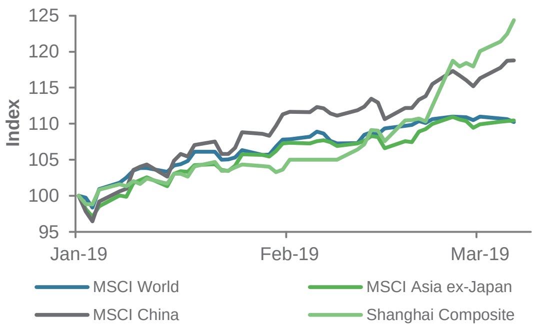
China stocks have outperformed global equities YTD

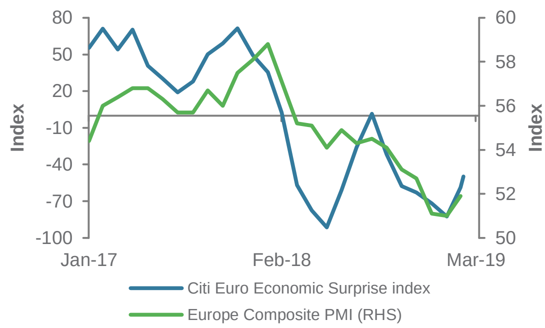
Relative performance of global, Asia ex-Japan, MSCI China and Shanghai Composite indices; 100=31-Dec-18



Source: Bloomberg, Standard Chartered

Euro area economic data appear to be stabilising

Euro area economic surprises index; Composite PMI



Source: Bloomberg, Standard Chartered

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What does this mean for investors?

Global equities pulled back after three weeks of gains, led by consolidation in US equities. Asia USD bonds outperformed in debt markets. The USD gained broadly, while gold pulled back.

Equities: US, European markets face near-term risks

- **US markets likely to consolidate near term.** The US equity rally has stalled after approximately 10% YTD gains. We believe key events, including a possible late-March US-China trade summit and 20 March Fed meeting, could lead to volatility. Although the market has priced in a US-China trade truce and no Fed rate hikes, any negative surprises (such as a hawkish Fed) could lead to a pullback. We believe consensus expectations for a 1% drop in Q1 US corporate earnings have likely been priced in, although a potential USD 800bn in share buybacks in 2019 could drive stocks higher. US equities remain a core holding.
- **Euro area earnings face downside risks.** Consensus forecasts indicate a 9% rise in Euro area corporate earnings in the coming 12 months, but we believe the lower-for-longer interest rate outlook could pose downside risks to net interest margins for the European banks sector. Also, Brexit uncertainty remains an overhang. Euro area equities remain least preferred, although we remain on watch for any positive surprises (such as a 'soft Brexit' or any improvement in economic data).

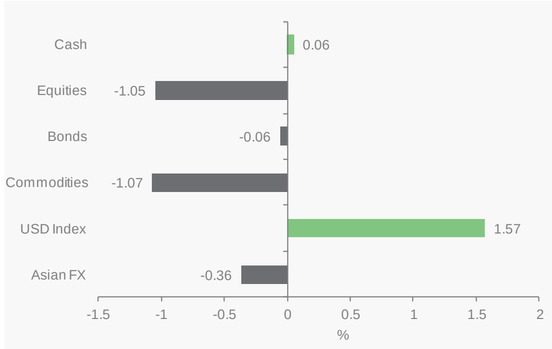
Bonds: Asia USD bonds buoyed by China stimulus

- **China measures boosts Asian bonds.** Asian USD bonds outperformed global bonds over the past week, likely helped by the slew of supportive measures announced by China. Bloomberg data indicates that demand has been strongest since 2016, substantially exceeding supply. While demand could moderate temporarily, we believe continued strong inflows remain supportive for EM USD government and Asian USD bonds, our preferred areas in bonds.
- **10-year Treasury yield faces key resistance.** The rebound last week in the US 10-year Treasury yield suggests it is attempting to form a base at 2.60-2.65%. However, the yield would need to break above key resistance at the January high of 2.80% for downward pressure to ease. Any break above 2.80% could put the yield back on a path towards the 3.0% mark, possibly higher.
- **Jobs data key to US yields.** In recent weeks, speculative positioning in favour of higher yields has increased and long-term inflation expectations have risen this year. The upcoming US jobs report is likely to be closely watched as strong wage growth is likely to be needed as a catalyst for yields to break higher.

FX: Remain short-term bearish on AUD

- **AUD/USD dragged by domestic economic outlook.** AUD/USD fell to a two-month low after Australia's weaker-than-expected Q4 GDP data increased expectations of a rate cut later this year. AUD's inability to capitalise on improving sentiment around US-China trade talks, rising iron ore prices and hopes of a recovery in Chinese growth later this year suggest the weakening domestic outlook is dominating investor sentiment. Although technical indicators suggest AUD/USD could be oversold, we remain bearish on the pair in the near term. Any break of support close to 0.7000 could pave the way towards the January low of 0.6750.
- **EUR/USD faces downside risk.** The EUR/USD slumped to its lowest since June 2017 following the ECB's dovish shift in policy. The magnitude of the fall suggests a decisive break below 1.1185-1.1213 would open up the possibility of a downward move towards 1.0865.

Benchmark (USD) performance w/w*



**Week of 28 February 2019 to 07 March 2019*

Source: MSCI, JP Morgan, DJ-UBS, Citigroup, Bloomberg, Standard Chartered (Indices used are JP Morgan Cash, MSCI AC World TR, Citi World Big, DJ-UBS Commodity, DXY and ADXY)

Asian equity market technicals remain strong

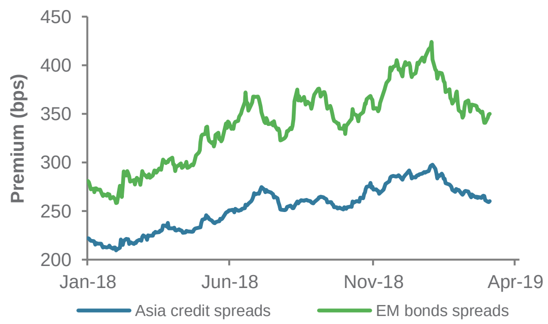
Technical levels of key market indicators as on 07 March

Index	Spot	1st support	1st resistance	Short-term trend
S&P500	2,749	2,680	2,817	↘
STOXX 50	3,309	3,261	3,347	↗
FTSE 100	7,158	7,000	7,360	↗
Nikkei 225	21,456	20,850	21,880	↗
Shanghai Comp	3,106	2,835	3,340	↑
Hang Seng	28,779	27,500	30,000	↑
MSCI Asia ex-Japan	654	635	683	↑
MSCI EM	1,044	1,029	1,075	↗
Brent (ICE)	66	61	72	↗
Gold	1,286	1,260	1,320	↘
UST 10Y Yield	2.64	2.62	2.82	↘

Source: Trading Central, Standard Chartered
Note: Arrows represent short-term trend opinions

Asia USD and EM USD bond yield premiums have continued to tighten amid rising fund inflows

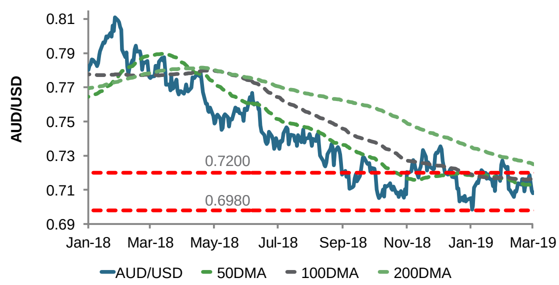
Yield premium over US Treasuries on Asia USD and EM USD government bond yields



Source: Bloomberg, Standard Chartered

AUD/USD faces key support close to 0.7000

AUD/USD



Source: Bloomberg, Standard Chartered

Top client questions

Q1. What are the key market implications of China's 2019 National People's Congress?

China's National People's Congress sent growth-supportive signals via further fiscal and monetary easing. The Government Work Report did not mention further deleveraging measures. Instead, the message was clear: large state-owned banks are to increase loans to small and medium enterprises by 30% to help ease credit. Also, Premier Li Keqiang announced a fiscal stimulus package with CNY 700-800bn worth of VAT cuts, an extra CNY 800bn in local government special bond issuance quotas and a 2-4ppt reduction in the social pension contribution for firms. The Government Work Report also said efforts will be stepped up to attract foreign capital by widening market access and opening the financial sector.

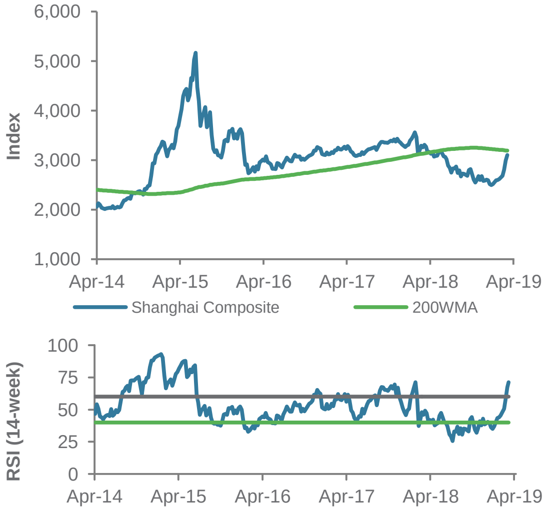
The overall tone was pragmatic, with a focus on supporting jobs and stabilising growth. Thus, we expect the monetary policy to remain accommodative over the coming year. Although the 2019 real GDP growth target was cut to 6.0-6.5% from "c.6.5%" in the past two years, this was largely in line with expectations. The larger-than-expected tax and fee cuts for manufacturing, transportation, construction and other industries was a positive surprise. Although the effective date for tax cuts is still to be announced, we believe the VAT cuts could boost MSCI China's 2019 earnings as companies pass on the tax cuts through lower sales prices, inducing more consumption. Meanwhile, the pro-market reform measures are likely to widen China's access to foreign capital, while tighter protection on intellectual property rights could help de-escalate US-China trade tensions.

Together, we believe these measures are potential medium- to long-term positive drivers for China equities, our preferred equity market in Asia. The measures are also supportive of our bullish outlook for Asia ex-Japan equities and Asia USD and EM USD government bonds.

The developments are especially positive for Asian USD bonds for two reasons. First, the increase in local government bond issuance quotas should marginally reduce bond supply and refinancing risk from local government financing vehicles (LGFVs) in the USD-denominated bond market. Second, the growth-supportive measures and tax cuts are credit-positives for Chinese bond issuers as likely improved earnings (due to tax cuts) and potentially lower onshore borrowing costs should help support fundamentals. Positive sentiment towards China should also have a spill-over impact on other Emerging Market (EM) economies and should act as a tailwind for EM USD government bonds.

The Shanghai Composite Index is close to a key technical resistance

Shanghai Composite Index and its 200-week-moving-average, weekly Relative Strength Index (RSI)



Source: Bloomberg, Standard Chartered

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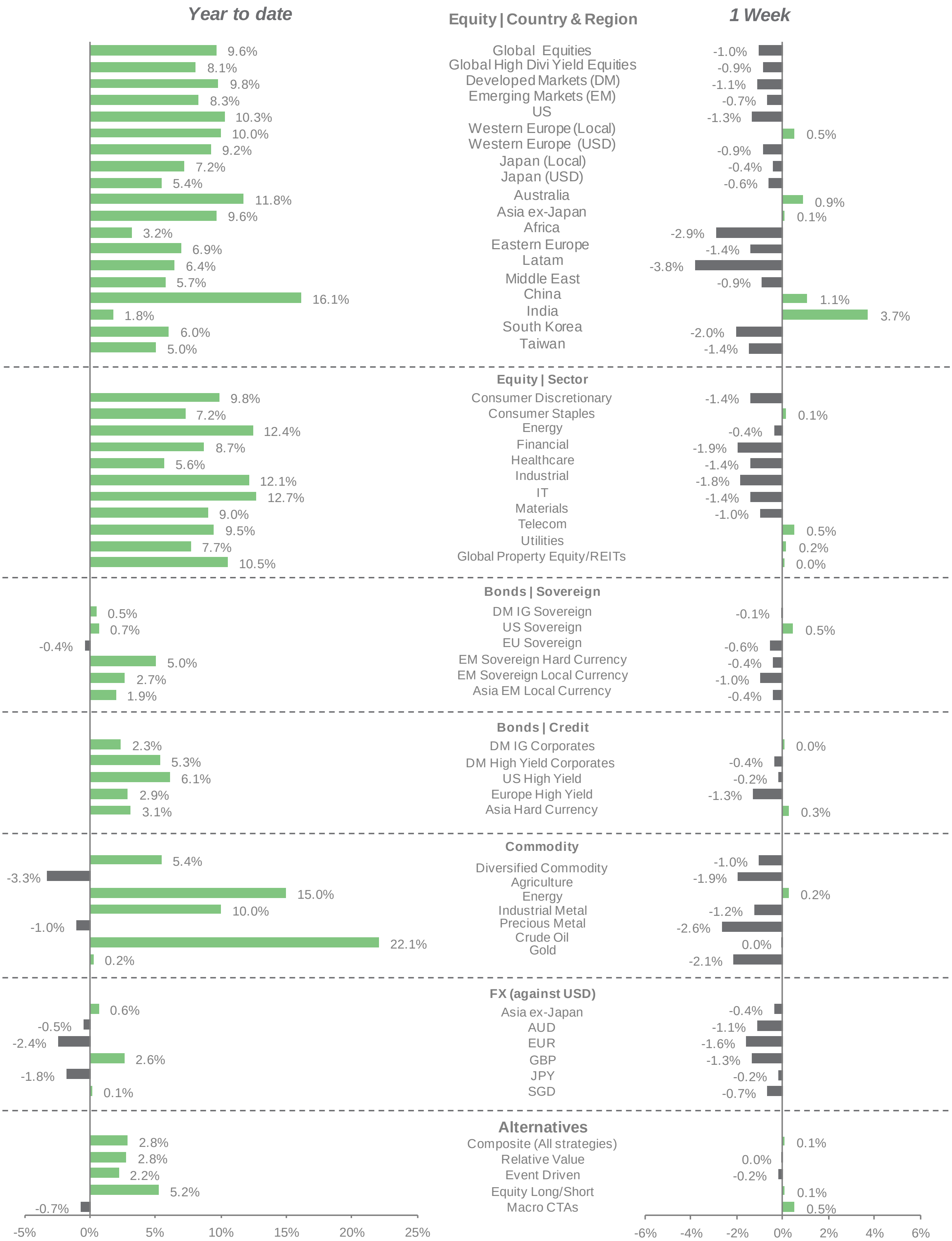
Market performance summary*



**Performance in USD terms unless otherwise stated, YTD period from 31 December 2018 to 07 March 2019, 1 week period: 28 February 2019 to 07 March 2019*

Sources: MSCI, JP Morgan, Barclays Capital, Citigroup, Dow Jones, HFRX, FTSE, Bloomberg, Standard Chartered

Economic & Market Calendar

	Event	Next Week	Date	Period	Expected	Prior
MON	GE	Industrial Production WDA y/y	11-Mar-19	Jan	-3.1%	-3.9%
	GE	Exports SA m/m	11-Mar-19	Jan	–	1.5%
	US	Retail Sales Ex Auto and Gas	11-Mar-19	Jan	0.6%	-1.4%
TUE	UK	GDP (m/m)	12-Mar-19	Jan	–	-0.4%
	US	CPI Ex Food and Energy y/y	12-Mar-19	Feb	2.1%	2.2%
WED	JN	Core Machine Orders y/y	13-Mar-19	Jan	–	0.9%
	US	PPI Ex Food and Energy y/y	13-Mar-19	Feb	–	2.6%
THUR	CH	Fixed Assets Ex Rural YTD y/y	14-Mar-19	Feb	6.0%	5.9%
	CH	Industrial Production YTD y/y	14-Mar-19	Feb	5.5%	6.2%
	CH	Retail Sales YTD y/y	14-Mar-19	Feb	8.2%	9.0%
FRI/SAT	US	Industrial Production m/m	15-Mar-19	Feb	0.8%	-0.6%
	US	U. of Mich. Sentiment	15-Mar-19	Mar P	95	93.8
	JN	BOJ Policy Balance Rate	15-Mar-19	3/15/2019	–	-0.1%
	IN	Exports y/y	15-Mar-19	Feb	–	3.7%

	Event	This Week	Date	Period	Actual	Prior
MON	SK	Nikkei South Korea PMI Mfg	4-Mar-19	Feb	47.2	48.3
	EC	Sentix Investor Confidence	4-Mar-19	Mar	-2.2	-3.7
	EC	PPI y/y	4-Mar-19	Jan	3.0%	3.0%
TUE	JN	Nikkei Japan PMI Composite	5-Mar-19	Feb	50.7	50.9
	CH	Caixin China PMI Composite	5-Mar-19	Feb	50.7	50.9
	AU	RBA Cash Rate Target	5-Mar-19	3/5/2019	1.5%	1.5%
	IN	Nikkei India PMI Composite	5-Mar-19	Feb	53.8	53.6
	UK	Markit/CIPS UK Composite PMI	5-Mar-19	Feb	51.5	50.3
	EC	Retail Sales y/y	5-Mar-19	Jan	0.3%	0.8%
	US	ISM Non-Manufacturing Index	5-Mar-19	Feb	59.7	56.7
WED	US	Trade Balance	6-Mar-19	Dec	-$59.8b	-$50.3b
THUR	US	Initial Jobless Claims	7-Mar-19	3/2/2019	223k	225k
	EC	ECB Main Refinancing Rate	7-Mar-19	3/7/2019	0.0%	0.0%
FRI/SAT	GE	Factory Orders WDA Y/y	8-Mar-19	Jan	–	-7.0%
	US	Change in Nonfarm Payrolls	8-Mar-19	Feb	–	304k
	US	Average Hourly Earnings Y/y	8-Mar-19	Feb	–	3.2%
	CH	Exports Y/y	8-Mar-19	Feb	–	9.1%

Previous data are for the preceding period unless otherwise indicated
Data are % change on previous period unless otherwise indicated
P - preliminary data, F - final data, sa - seasonally adjusted
y/y – year-on-year, m/m - month-on-month

Source: Bloomberg, Standard Chartered; key indicators highlighted in blue

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