Standard Chartered
Private Bank

weekly market view

macro strategy | 22 March 2019

This reflects the views of the Wealth Management Group

Editorial

Lift from Fed, but trade outlook cloudy

- **The Fed's decisively dovish policy turn is positive for global risk assets. However, expectations from US-China trade talks have softened.**
- **Equities:** Emerging Markets, especially in Asia ex-Japan, are likely to be the biggest beneficiaries of the Fed's dovish pivot.
- **Bonds:** We expect continued inflows into EM bonds following the Fed's dovish stance. EM USD government bonds and Asia USD bonds are likely to be key beneficiaries.
- **FX:** The USD slumped after the Fed eased its rate projections. We see rising risk of further downside.

What's new?

- **Lift from the Fed.** The Fed eased its monetary policy stance by more than the market expected. It now projects no rate hikes in 2019 (versus the December 2018 forecast of two hikes). The central bank also moderately lowered US growth and inflation estimates for 2019-20 and said it would end its balance sheet reduction programme by September. Fed Chair Powell said global trade tensions, slowing growth in Europe and China and uncertainty around the Brexit warranted a patient stance. The Fed's dovish policy shift is likely to enable other global central banks, especially in Emerging Markets (EMs), to turn more accommodative. When combined with China's increasingly pro-growth policy measures and the ECB's recent guidance of a prolonged accommodative stance, we believe the global policy environment has turned increasingly supportive for risk assets. See page 3 for more on investment implications.
- **Trade outlook remains uncertain.** US President Trump dampened expectations of an imminent US-China trade deal, saying existing tariffs against imports from China will remain for a "substantial period of time" to make sure China complies with any trade agreement. This raises the prospect of a pushback from China, delaying any such agreement. Nevertheless, we believe this is unlikely to hold back equity markets as long as trade talks continue and tensions do not escalate. Asia ex-Japan remains our preferred regional equity market, with China onshore and offshore equities preferred within the region.
- **Dovish Fed to weigh on USD, especially vs GBP.** The Fed's dovish turn in policy led to a broad-based pullback in the USD. Downside risk has risen amid narrowing interest rate differentials between the US and other major economies. The GBP is likely to be the biggest beneficiary, as it benefits from receding concerns about a hard Brexit. Although the UK-EU talks may go down to the wire (ie, 29 March, when the UK is scheduled to leave the EU), we believe both sides are keen to avoid the UK leaving without an agreement. EU leaders agreed to a delay in Brexit, either until 22 May if the UK parliament approves the existing withdrawal deal, or until 12 April if it rejects the current deal. The latter outcome could lead to a referendum or an election, which would likely be medium-term positive for the GBP.

What we are watching

- a) A likely third vote by the UK parliament on Brexit deal, b) US-China trade talks, and c) US' decision on auto import tariffs.

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Fed cut its forecasts for US growth and inflation moderately and rate forecasts significantly, which, we believe is positive for global risk assets

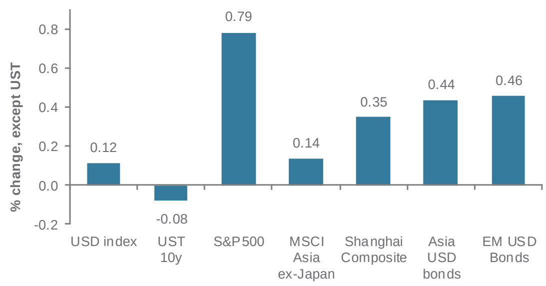
Fed's latest projections for US growth, inflation, unemployment and interest rates

Variable	Median (%) 2019	2020	2021	Longer run
Real GDP growth	2.1 (2.3)	1.9 (2.0)	1.8 (1.8)	1.9 (1.9)
Unemployment rate	3.7 (3.5)	3.8 (3.6)	3.9 (3.8)	4.3 (4.4)
PCE inflation	1.8 (1.9)	2.0 (2.1)	2.0 (2.1)	2.0 (2.0)
Core PCE inflation	2.0 (2.0)	2.0 (2.0)	2.0 (2.0)	–
Median Fed funds rate	2.4 (2.9)	2.6 (3.1)	2.6 (3.1)	2.8 (2.8)

Source: Bloomberg, Standard Chartered

Fed's dovish pivot weighed on the USD and Treasury yields and boosted US stocks and EM assets

Performance of various assets since the Fed's decision on 20 March; USD index, US Treasury yield (ppt) and S&P500 are for 20-21 March, rest are for 21 March



Source: Bloomberg, Standard Chartered

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What does this mean for investors?

Global stocks, bonds and commodities rallied and USD slumped after the Fed's more-dovish-than-expected policy outlook. EMs outperformed Developed Markets in equities and bonds. Asian currencies gained amid expectation of increased inflows.

Equities: Fed's dovish pivot is positive for EM equities

- **Fed's stance likely to boost EM inflows.** The Fed's projection for no rate hikes in 2019 has positive implications for global equity markets. While there are concerns about US economic growth, and in turn earnings, lower bond yields help partially offset this (as it makes expected equity returns more attractive vs. bonds). This trend, in combination with survey data that shows a currently neutral fund manager stance towards global equities, implies that any pullback in markets is likely to be short-lived as high cash positions are reduced and put to work in equity markets. We prefer Asia ex-Japan, though most EM equities should benefit.
- **Euro area equities continued their recovery** from the 2018 sell-off, performing almost in line with global equities YTD. Lower peripheral bond yields as well as a dovish pivot by the ECB has fuelled optimism. Nevertheless, weakness in the Euro area banking sector, reinforced by the dovish tone of global central banks, is likely to act as a ceiling on gains this year, in our view.

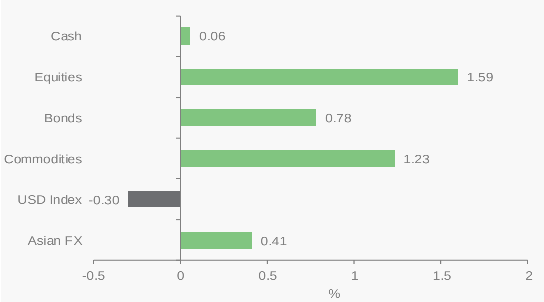
Bonds: Tailwind for EM bonds

- **Fed pause to cap yields:** US 10-year Treasury yields fell around 8bps since the Fed meeting, well below the key technical support of 2.62%. Fed's expectations of no rate hikes in 2019 and reduced inflation concerns are likely to help keep yields below 2.75% for an extended period of time.
- **Tailwind for EM bonds:** EM USD bonds delivered strong returns, helped by lower Treasury yields, while EM local currency bonds were helped by a weaker USD. Asian bond yield premiums also continued to decline. A more accommodative Fed is likely to be beneficial for EM bonds, as it encourages more inflows into EM assets. Lower Treasury yields should also cap the interest servicing burden and, at the margin, support credit worthiness of EM bond issuers. Both factors provide further support to our preference for EM USD government and Asian USD bonds.

FX: GBP faces near-term risk, medium-term upside

- **GBP/USD momentarily broke below its trend-line support** (1.3035). We see strong support at 1.2910-1.2950. Near-term uncertainty around Brexit may keep volatility elevated over the coming week, but should a 'no-deal Brexit' be avoided, we believe GBP/USD could retest levels around 1.3380-1.3405. We expect further upside over the medium term, initially towards 1.40 and then towards 1.45, as the market starts anticipating a no-Brexit outcome, perhaps after a referendum or an election.
- **EUR/USD gets a lift from a dovish Fed.** The EUR broke above its downtrend line around 1.1360 and tested its end-February high at 1.1420, as the USD weakened following the Fed's decision. We turn more constructive on the pair over the next three months amid narrowing rate differentials between the US and Europe. However, the pair faces a strong near-term resistance at 1.1420-1.1450 and the 200DMA close to 1.1475.
- **Although AUD/USD broke above the 100DMA**, our bearish bias holds. Leading indicators are pointing to a slowdown in jobs growth. Business confidence and conditions have also weakened. We expect AUD/USD to weaken and re-test 0.7050 in the coming days.

Benchmark (USD) performance w/w*



**Week of 14 March 2019 to 21 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)

US and Asia equity technical indicators are strong

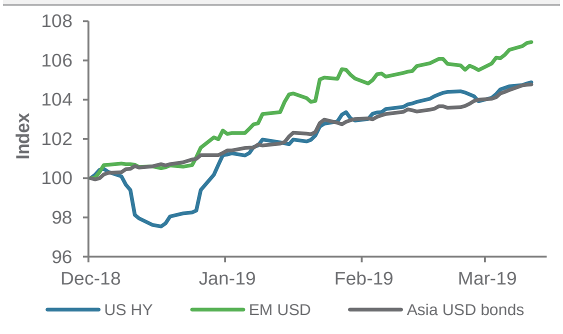
Technical levels of key market indicators as on 21 March

Index	Spot	1st support	1st resistance	Short-term trend
S&P500	2,855	2,790	2,900	↑
STOXX 50	3,367	3,319	3,430	↘
FTSE 100	7,355	7,210	7,390	↗
Nikkei 225	21,609	20,950	21,880	↑
Shanghai Comp	3,101	2,930	3,230	↑
Hang Seng	29,072	28,200	30,000	↑
MSCI Asia ex-Japan	665	635	683	↑
MSCI EM	1,070	1,027	1,097	↗
Brent (ICE)	68	63	72	↑
Gold	1,308	1,280	1,320	↘
UST 10Y Yield	2.54	2.40	2.71	↘

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

EM USD government bonds outperformed US HY and Asia USD bonds over the past three months; Fed's dovish turn to likely sustain outperformance

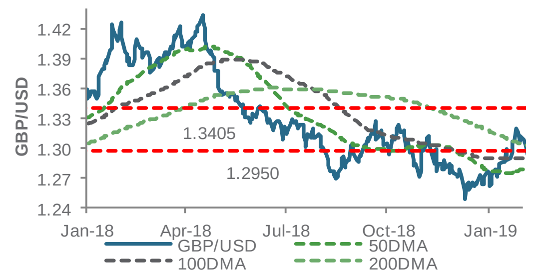
Relative performance of EM USD government bond, US HY and Asia USD bond indices since we published Outlook 2019 (10 December 2018)



Source: Bloomberg, Standard Chartered

GBP is likely to be the biggest gainer from any USD weakness as Brexit uncertainty gradually recedes

GBP/USD



Source: Bloomberg, Standard Chartered

Top client questions

Q1. What are the market implications for the Fed's dovish policy pivot?

We believe the Fed's latest cuts in projected interest rates through 2020 are positive for global risk assets, especially EM equities and bonds. Here we outline the implications for key asset classes.

Bonds: The dovish shift from the Fed is largely positive for bonds. We see increased probability that US 10-year Treasury yields may remain below 2.75% over the next 12 months. US Investment Grade (IG) and corporate bonds could benefit, as lower government bond yields are likely to drive demand for corporate bonds, which offer higher yields. At the same time, a reduction in the borrowing cost is likely to reduce pressure on credit quality. EM bonds are likely to be the biggest beneficiaries, as a more accommodative Fed could keep the USD capped. This, combined with higher EM growth and attractive yields, is likely to drive substantial inflows into EM bonds, in our view. We continue to prefer EM USD government, followed by Asian USD bonds, within bonds.

FX: The USD slumped in reaction to a dovish Fed. The key question for the USD is how other global central banks will react. We note the Fed pivot in January heralded a wave of dovish policy tilts worldwide. We believe many central banks, especially in EMs, may not be comfortable with the prospect of a much stronger currency against the USD.

In the near term, increased USD liquidity is likely to support EM currencies, and unless there is a pushback from other central banks or a significant setback to US-China trade talks, the Fed's current policy shift is likely to result in a broadly weaker USD.

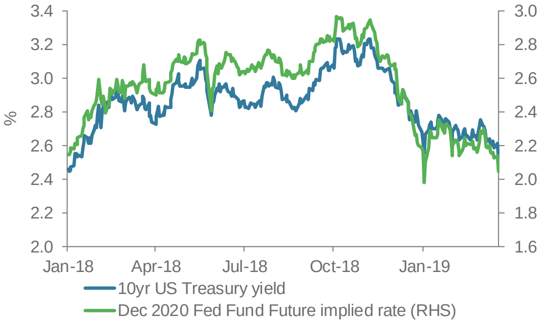
The USD Index (DXY) is close to its 200DMA at 95.85, and a sustained break would see a test of the 95.00 area – the low of early January and a key level for near-term USD sentiment, which has held the 95.00-98.00 sideways channel since last October. The key level for the medium-term trend sits at 93.80-94.10. A break here would suggest a move back towards the 90.00-92.00 region.

Equities: Equity markets have benefited from a series of tailwinds in 2019, including dovish central banks and easing of US-China trade tensions. These factors have helped offset concerns about slowing US earnings growth. This positive trend has been reinforced by the Fed's latest dovish pivot. However, US-China trade negotiations could extend further as President Trump insists on China's compliance with the terms of any initial agreement, before rolling back existing tariffs. We continue to believe that US and China will reach a compromise, enabling the eventual reduction in trade tariffs by both sides. This leaves us constructive on global risk assets, especially Asia ex-Japan stocks, our preferred region within equities.

Among sectors, technology and energy are the top-performing areas YTD, despite forecasts of slower earnings growth. We square this circle by observing that the one-off positives related to tax cuts last year created a high statistical base effect that would always be difficult to top. As such, we believe there is value in looking through the downturn in earnings and focusing on the underlying strength in both sectors, both of which are preferred.

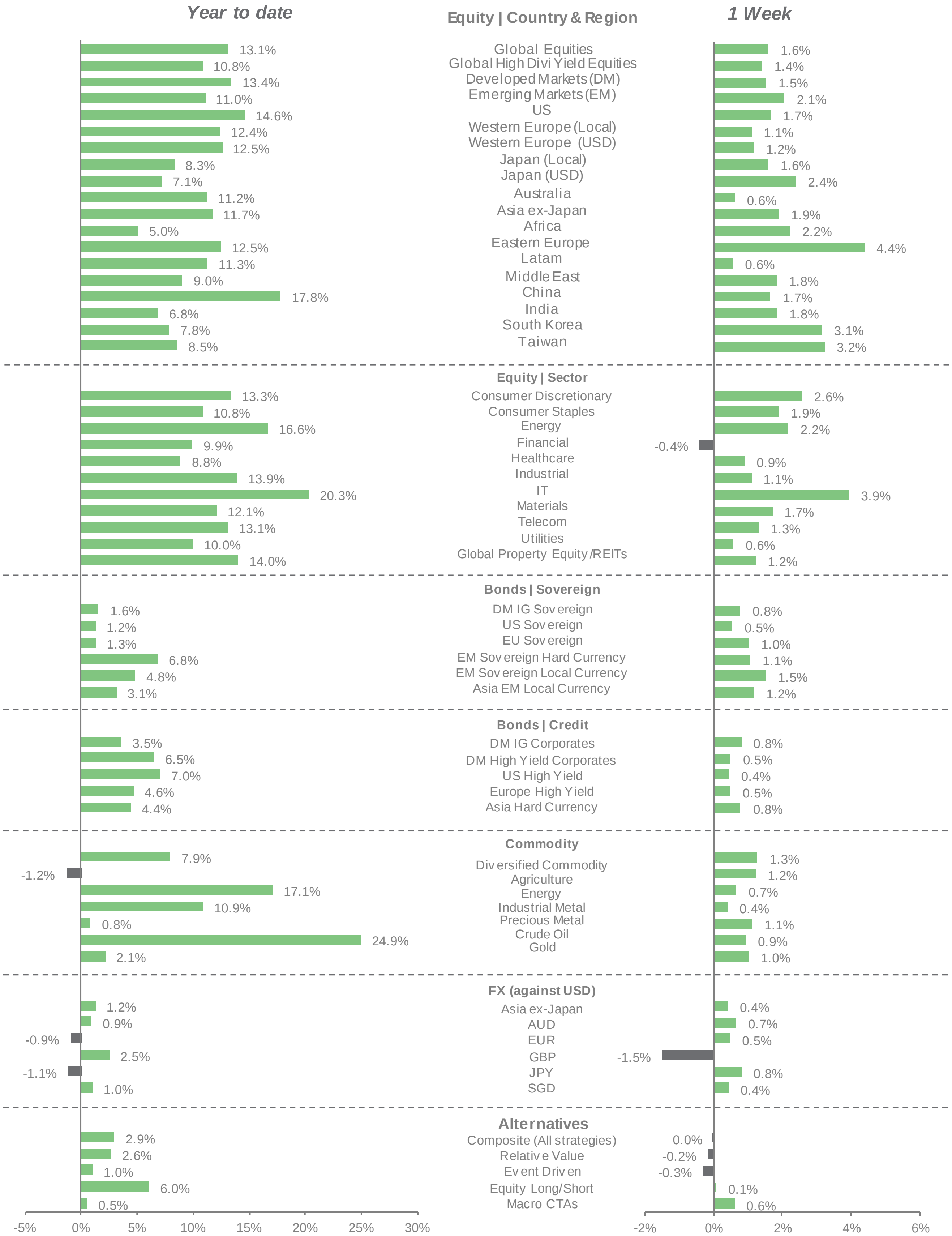
US Treasury yields have been dragged lower by waning expectations of any Fed rate hike this year

US 10-year Treasury yields; December 2020 Fed Fund future implied rate



Source: Bloomberg, Standard Chartered

Market performance summary*



*Performance in USD terms unless otherwise stated, YTD period from 31 December 2018 to 21 March 2019, 1 week period: 14 March 2019 to 21 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	IFO Expectations	25-Mar-19	Mar	94.5	93.8
TUE	US	Housing Starts	26-Mar-19	Feb	1225k	1230k
	US	Building Permits	26-Mar-19	Feb	1320k	1317k
	US	Conf. Board Consumer Confidence	26-Mar-19	Mar	132.0	131.4
WED	CH	Industrial Profits y/y	27-Mar-19	Feb	–	-1.9%
THUR	EC	Economic Confidence	28-Mar-19	Mar	–	106.1
	US	GDP Annualized q/q	28-Mar-19	4Q T	2.4%	2.6%
	US	Initial Jobless Claims	28-Mar-19	23-Mar	–	–
	GE	CPI EU Harmonized y/y	28-Mar-19	Mar P	1.7%	1.7%
FRI/SAT	EC	CPI Core y/y	29-Mar-19	Mar A	–	1.0%
	US	Personal Income	29-Mar-19	Feb	0.3%	-0.1%
	US	PCE Core y/y	29-Mar-19	Jan	–	1.9%
	US	Chicago Purchasing Manager	29-Mar-19	Mar	61.7	64.7
	US	New Home Sales	29-Mar-19	Feb	617k	607k

	Event	This Week	Date	Period	Actual	Prior
MON	JN	Exports y/y	18-Mar-19	Feb	-1.2%	-8.4%
TUE	UK	Average Weekly Earnings 3m/ y/y	19-Mar-19	Jan	3.4%	3.4%
WED	UK	CPI Core y/y	20-Mar-19	Feb	1.8%	1.9%
THUR	US	FOMC Rate Decision (Upper Bound)	21-Mar-19	20-Mar	2.5%	2.5%
	UK	Retail Sales Ex Auto Fuel y/y	21-Mar-19	Feb	3.8%	4.1%
	UK	Bank of England Bank Rate	21-Mar-19	21-Mar	0.75%	0.75%
	US	Initial Jobless Claims	21-Mar-19	16-Mar	221k	229k
	US	Leading Index	21-Mar-19	Feb	0.2%	0.0%
	EC	Consumer Confidence	21-Mar-19	Mar A	-7.2	-7.4
FRI/SAT	JN	Natl CPI Ex Fresh Food, Energy y/y	22-Mar-19	Feb	0.4%	0.4%
	JN	Nikkei Japan PMI Mfg	22-Mar-19	Mar P	48.9	48.9
	GE	Markit/BME Germany Composite PMI	22-Mar-19	Mar P	–	52.8
	EC	Markit Eurozone Composite PMI	22-Mar-19	Mar P	–	51.9
	US	Markit US Composite PMI	22-Mar-19	Mar P	–	55.5
	US	Existing Home Sales	22-Mar-19	Feb	–	4.94m

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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