

Market Watch

A healthy moderation

Summary

Global stocks slumped, led by the US, where the S&P500 index erased gains for the year. A pullback was anticipated (as we alerted in recent weeks), given crowded positions in equity markets.

We see this as a healthy pullback after a sharp rally, especially after the November US elections. The S&P500 index has immediate support 4% below current levels and stronger support 11% from here.

Fundamental drivers of the uptrend remain unchanged, although technical/positioning factors, including hedge fund deleveraging, could last for a few days. **We would view a deeper pullback as an opportunity to average into our preferred themes.**

Background

In the US, the S&P500 and Nasdaq Composite indices both fell 2.6%. The S&P500 volatility index, a measure of risk sentiment, surged to 37%, its highest since October. The broad USD rose 0.5% and US 10-year Treasury yields fell 2bps to 1.02%.

Communication Services, Consumer Discretionary and Healthcare sectors led yesterday's decline in the S&P500 index, all three losing more than 3%.

Hedge fund deleveraging, profit-taking and concerns about slower-than-expected vaccinations are some of the likely reasons behind the pullback.

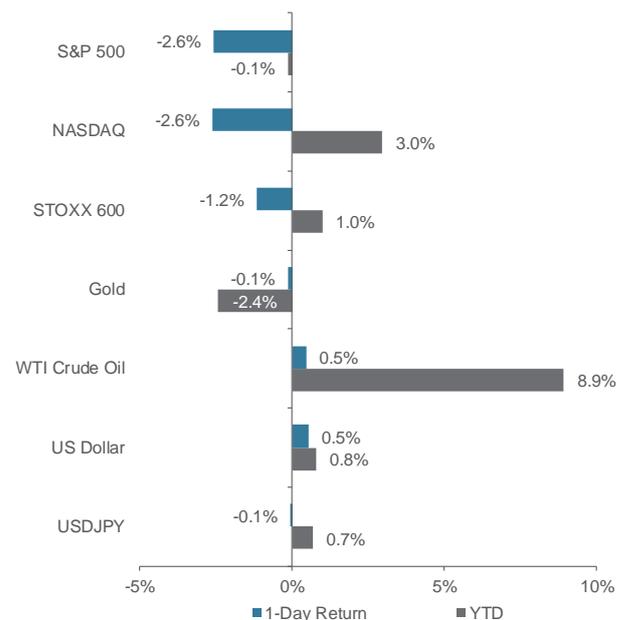
What does this mean for investors?

Charts suggest more near-term downside. A break below the mid-January low of 3750 for the S&P500 index would signal that near-term uptrend has likely faded. The next support is 4% lower at 3588, followed by a much stronger support at 3341, 11% lower.

Corporate earnings, policy remain fundamental support for risk assets in the medium term. The Fed's reiteration of its lower-for-longer interest rates policy and US Q4 earnings beats support this view.

US stocks led the pullback in risk assets

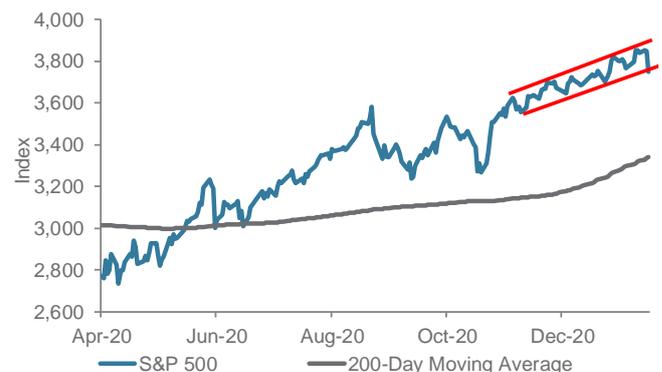
Performance of selected asset classes on 27-Jan



Source: Bloomberg, Standard Chartered

The S&P500 index is testing the lower end of its uptrend channel

S&P500 index



Source: Bloomberg, Standard Chartered

Trends to watch

Hedge fund deleveraging. Crowded positions and stretched technical indicators meant equities needed only a catalyst for a reversal. Reported deleveraging by some hedge funds was likely a catalyst in the latest pullback amid concerns about whether this may broaden selling pressure as funds rebalance. While this deleveraging due to the so-called short-squeeze could last for a few more days, we believe longer-term investors are likely to use the latest correction as an opportunity to add exposure to equities.

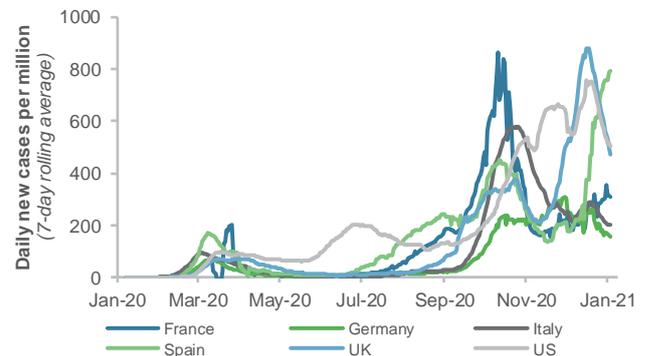
Monetary policy remains highly supportive. The Fed reiterated yesterday that it plans to maintain its current highly accommodative policy, including USD 120bn of monthly bond purchases, for the foreseeable future until job markets recover and long-term inflation sustainably rises above its 2% target. Although some investors may be disappointed that the Fed did not add further support, we believe the monetary policy backdrop is likely to remain highly supportive for risk assets over the current year.

Biden's 100-day vaccination and fiscal stimulus implementation. The US President has targeted 100 million vaccinations in the first 100 days in office. He has stepped up purchase and distribution of vaccines, which we believe will lead to an acceleration in inoculations in the coming days. US daily new COVID-19 cases are also on the downtrend. Biden's USD 1.9tn fiscal stimulus package is also in focus. We expect the administration to get enough support in the Congress to approve at least half of that package by March, including USD 1,400 cheques for most Americans. This would be positive for US consumption and growth.

Technical charts still positive medium-term. The S&P 500 is now testing key support on the lower edge of the channel and the mid-January low of 3750. On its own, Wednesday's drop isn't enough to conclude that a correction is imminent (note a similar drop occurred on January 4). The index could well rebound from the lower edge of the channel, as it has done so earlier this month. However, a daily close below the support would confirm that the upward pressure had faded in the short term. Subsequent support is at the September high of 3588 (4% from Wednesday's close). **Strong support is on the 200-day moving average (now at 3341; 11%).**

New COVID-19 cases are on the decline in most major economies

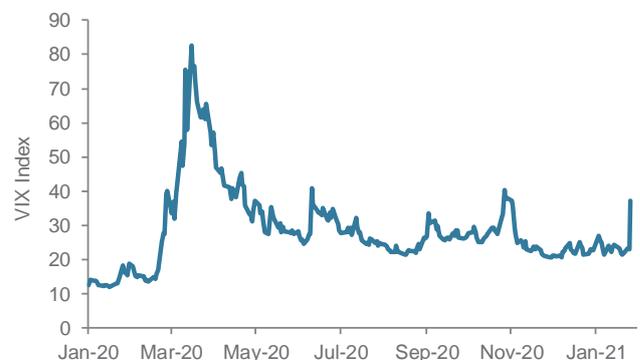
Daily new COVID-19 cases across major economies



Source: Our World in Data, Standard Chartered

S&P500 index volatility has risen to levels last seen around the US elections

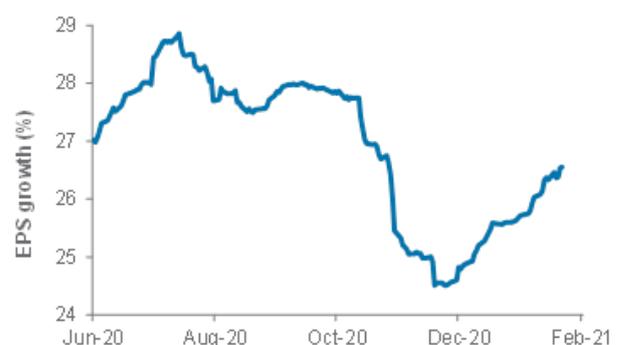
S&P500 volatility index (VIX)



Source: Bloomberg, Standard Chartered

Expectations of a global corporate earnings rebound in 2021 has strengthened in recent weeks

Consensus expectations of 2021 earnings growth for global equities



Source: MSCI, FactSet, Standard Chartered

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