

weekly market view

macro strategy | 14 December 2018

This reflects the views of the Wealth Management Group

Editorial

This is our final Weekly for 2018. We will resume publication on 11 January 2019. We wish readers a Happy New Year!

Preparing for tactical opportunities

- **We continue to prefer a broadly diversified allocation. Within this, we believe Asia-ex-Japan equities and Emerging Market (EM) government bonds offer tactical opportunities.**
- **Equities:** We prefer the energy sector in the US and Euro area on the back of our positive oil price view. Continued progress in US-China trade talks would be positive for China equities.
- **Bonds:** Any signal from the Fed that it may pause rate hikes after its 18-19 December meeting is likely to be particularly bullish for EM USD government bonds.
- **FX:** GBP/USD rebounded from a 20-month low after PM May survived a no-confidence vote. The next resistance is at 1.2925.

What's new?

- **China takes measures to ease US trade rift.** The revival of high-level talks, after President Trump and President Xi agreed to a 90-day trade truce, has helped partly ease concerns about further escalation. China has also announced measures aimed at narrowing its trade surplus with the US, including restarting imports of US LNG and soybeans. There is also talk of cutting auto import tariffs to 15% from 40%. Reports suggest Beijing is also revising its 'Made in China 2025' plan (aimed at making the country a technology leader) to ease US concerns about its technology acquisition strategy. Although these positive measures were partly offset by the arrest of a top Chinese technology executive in Canada, we believe the two sides are keen to resolve their disputes before it damages the outlook for both economies. Any signs of a resolution would be positive for Asia ex-Japan stocks in the near term (see chart on right).
- **ECB stays cautious.** The central bank confirmed it was ending its bond buying programme, but cut its growth and inflation forecasts for 2019 amid further signs of a slowdown in the Euro area economy (both Sentix Investor Confidence and Zew Survey Expectations for growth fell to multi-year lows). Markets are now pricing the first rate hike in Q1 2020. Although there were signs of progress in EU's budget talks with Italy, the ongoing French populist protests are likely to put upward pressure on the French budget deficit as President Macron announced tax cuts and minimum wage hikes. The region's economic challenges underscore why we rank Euro area equities as least-preferred.
- **GBP jumps as May survives vote.** The GBP rebounded from a 20-month low after Prime Minister May won a no-confidence vote. The premier's next challenge is to get parliament's approval for her Brexit plan (as agreed with the EU), a likely tougher task than winning the confidence vote. If GBP/USD recovers this week's losses and breaks early-December highs around 1.2850, it could signal that the medium-term downtrend is easing. Any failure to break higher could lead to a retest of this week's lows around 1.2475. The 1.20 level remains a strong psychological support.

What we are watching

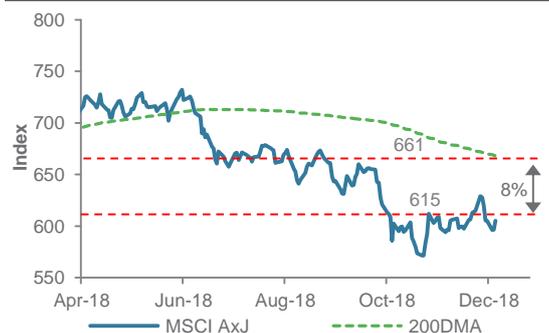
- **Fed meeting.** Any signals from the meeting of a pause in rate hikes would be positive for global equities and EM assets.

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The MSCI Asia ex-Japan equity index has so far been unable to sustainably break above the November-high of 615; a break could lead to an 8% gain

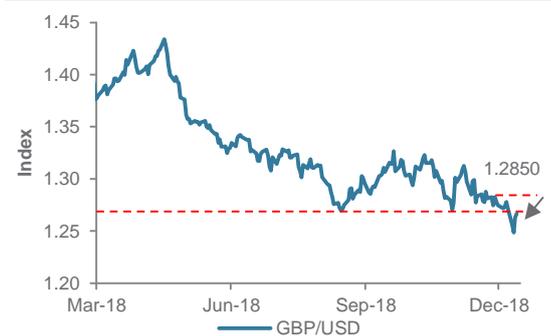
MSCI Asia ex-Japan index



Source: Bloomberg, Standard Chartered

GBP/USD rebounded from a 20-month low; any break above the December high of 1.2850 could signal an easing in the medium-term downtrend

GBP/USD



Source: Bloomberg, Standard Chartered

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What does this mean for investors?

Global equities extended declines, although Asian equities and EM bonds gained amid signs of easing US-China trade tensions. Crude oil rebounded after OPEC and Russia agreed to cut output.

Equities: Tactical opportunities in select sectors

- **Energy and healthcare sectors preferred in the US and Euro area.** We expect Brent crude oil prices to rebound to a USD 65-75/bbl range over the next 12 months after OPEC and Russia agreed to cut their combined crude oil output by 1.2mbpd. The expected rebound is likely to boost energy sector equities after they suffered a 15-20% peak-to-trough drop in Q3. Our preference for the healthcare sector reflects our strategy to balance our cyclical exposure (to oil) with a more defensive sector. Healthcare is also less impacted by trade tensions.
- **The US financial sector remains under pressure,** with banks leading declines. Expectations of a slower pace of Fed rate hikes in 2019 are weighing on expected net interest margins. Slower economic activity could also negatively impact loan growth and bank fee-based income. Consensus expectations in 2019 are for 10% earnings growth in the financial sector, down from the 30% forecast for 2018. As a result, we see the financial sector in the US and Euro area as a core holding, rather than preferred.
- **Prefer utilities in China.** The arrest of a leading Chinese technology executive in Canada has renewed concerns of possible escalation in US-China tensions. Market turnover in Hong Kong and China has shrunk, likely due to the uncertainty. Also, the roll-out of new policies arising from US-China trade negotiations has affected sentiment, with the proposed tariff cut for auto imports into China raising competition concerns and hurting the auto sector. Hence, in China, we prefer the utilities sector given it is likely less affected by trade tensions.

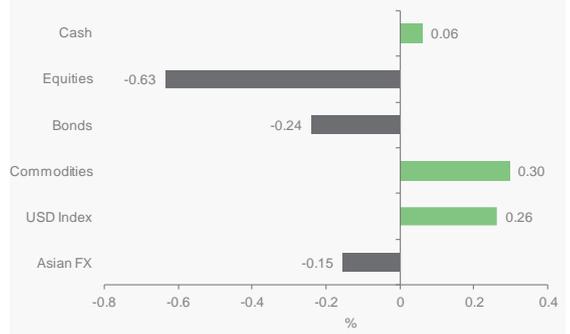
Bonds: Focus on the Fed

- **The 10-year US Treasury yield bounced-off key technical support at 2.81%.** We expect the Fed to hike rates next week and twice more in 2019, which is more than the current market expectation (see chart). We believe this adjustment of expectations may help drive yields modestly higher, likely back above 3.00%, over the next few months.
- **EM USD government bonds, our preferred bonds asset class,** outperformed over the past week as yield premiums declined owing to improved risk sentiment. Despite the recent rally, EM USD government bonds continue to offer attractive relative value and overall yield, in our opinion. Asian USD bonds, a core holding for us, were largely flat as higher-than-expected supply led to a slight increase in yield premiums. We continue to view Asian USD bonds, especially Investment Grade (IG) bonds, as a core holding owing to their relatively high credit quality and low volatility.

FX: USD shows signs of fatigue

- **No signs yet of a reversal in the uptrend.** The multi-month USD rally continued to show signs of fatigue around the August-high of 96.98. However, the loss of momentum has not been associated with a price confirmation (such as break of a technical support level). The early November low of 95.68 is an important support. A break below the support would indicate that the upward pressure has eased. In the absence of any bearish evidence, the broad USD trend remains up. The weakness in EUR/USD on the back of a dovish ECB outlook is likely to add further support to the USD. We believe the EUR/USD is likely to test its support at 1.1190 in the near-term.

Benchmark (USD) performance w/w*



*Week of 06 December 2018 to 13 December 2018

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 equity market technicals have turned positive

Technical levels of key market indicators as on 13 Dec

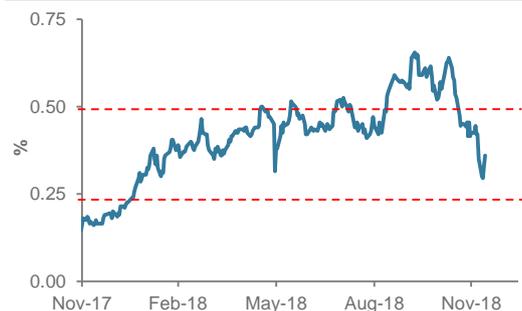
Index	Spot	1st support	1st resistance	Short-term trend
S&P500	2,651	2,600	2,710	↗
STOXX 50	3,112	2,950	3,151	↘
FTSE 100	6,878	6,570	7,010	↘
Nikkei 225	21,816	20,960	22,040	↘
Shanghai Comp	2,634	2,552	2,690	↘
Hang Seng	26,524	25,600	26,700	↘
MSCI Asia ex-Japan	611	568	619	↘
MSCI EM	986	930	1,008	↘
Brent (ICE)	61	58	65	↘
Gold	1,242	1,230	1,255	↗
UST 10Y Yield	2.91	2.80	3.04	↘

Source: Trading Central, Standard Chartered

Note: Arrows represent short-term trend opinions

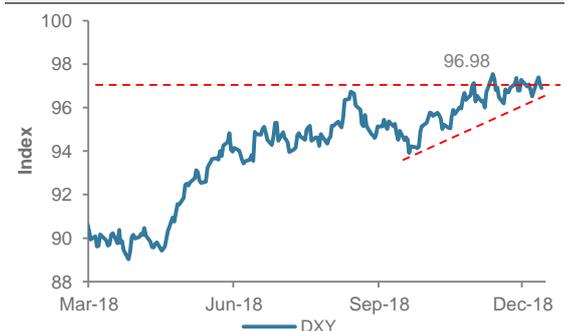
Although market expectations of Fed rate hikes have eased to just over one 25bps hike in 2019, we expect two increases (which would support Treasury yields)

Market expectations of Fed rate hikes



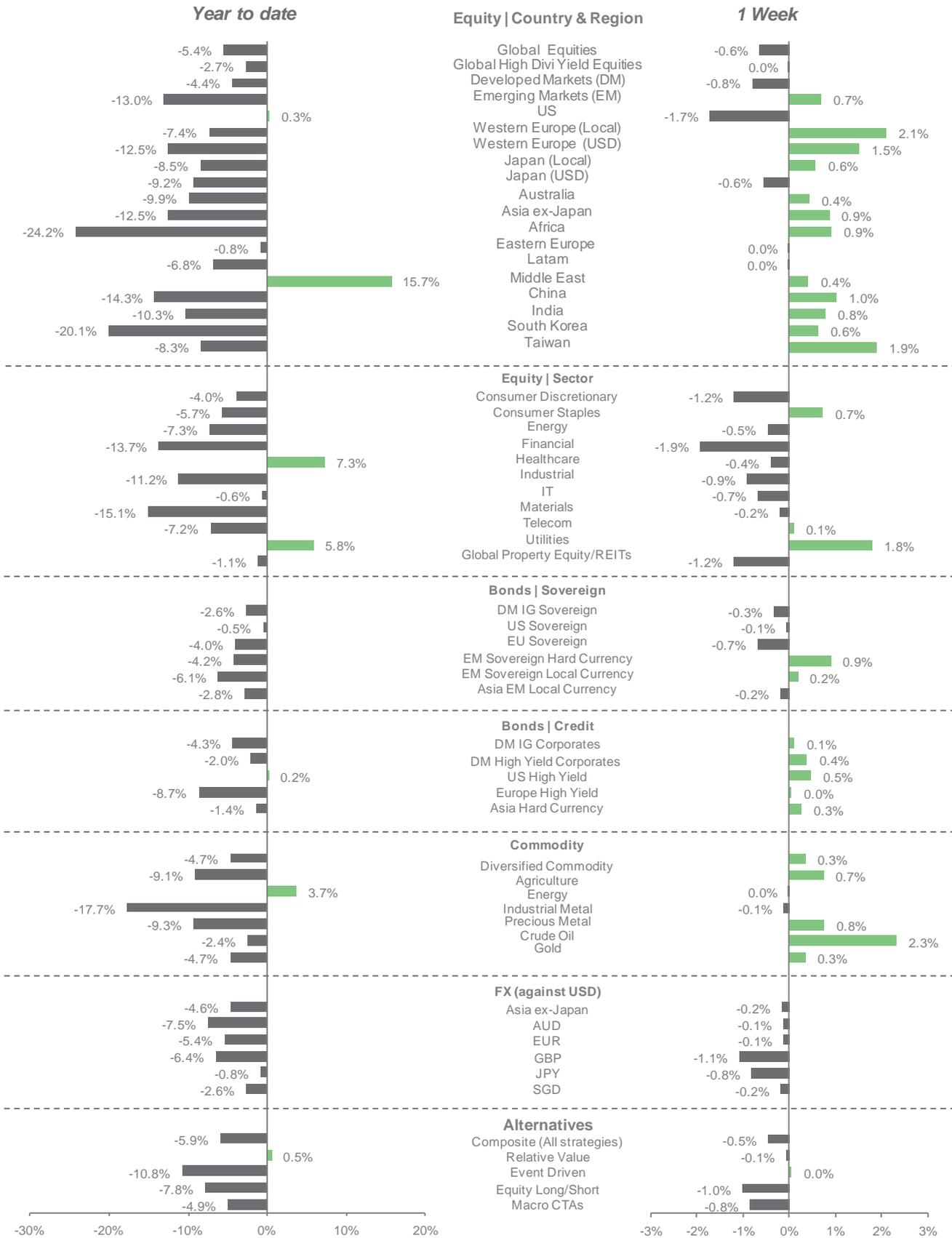
Source: Bloomberg, Standard Chartered

The broad USD uptrend is showing signs of fatigue, although it has remained above key support levels USD (DXY) index



Source: Bloomberg, Standard Chartered

Market performance summary*



*Performance in USD terms unless otherwise stated, YTD period from 31 December 2017 to 13 December 2018, 1 week period: 06 December 2018 to 13 December 2018

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

Economic & Market Calendar

	Event	Next Week	Date	Period	Expected	Prior
TUE	US	Building Permits	18-Dec-18	Nov	1265k	1265k
	US	Housing Starts	18-Dec-18	Nov	1230k	1228k
	JN	Exports y/y	18-Dec-18	Nov	1.9%	8.2%
WED	UK	CPI y/y	19-Dec-18	Nov	–	2.4%
	US	Existing Home Sales	19-Dec-18	Nov	5.20m	5.22m
	JN	BOJ Policy Balance Rate	19-Dec-18	20-Dec	–	-0.1%
	US	FOMC Rate Decision (Upper Bound)	19-Dec-18	19-Dec	2.5%	2.3%
THUR	EC	ECB Current Account SA	20-Dec-18	Oct	–	16.9b
	UK	Bank of England Bank Rate	20-Dec-18	20-Dec	–	0.8%
	UK	BOE Asset Purchase Target	20-Dec-18	Dec	–	435b
FRI/SAT	US	Cap Goods Orders Nondef Ex Air	21-Dec-18	Nov P	–	0.0%
	US	Personal Consumption	21-Dec-18	3Q T	–	3.6%
	EC	Consumer Confidence	21-Dec-18	Dec A	–	-3.9
	US	PCE Core y/y	21-Dec-18	Nov	1.8%	1.8%
	US	Personal Income	21-Dec-18	Nov	0.3%	0.5%

	Event	This Week	Date	Period	Actual	Prior
MON	GE	Exports SA m/m	10-Dec-18	Oct	0.7%	-0.4%
	EC	Sentix Investor Confidence	10-Dec-18	Dec	-0.3	8.8
	UK	Manufacturing Production y/y	10-Dec-18	Oct	-1.0%	0.5%
TUE	EC	ZEW Survey Expectations	11-Dec-18	Dec	-21.0	-22.0
	US	PPI Ex Food and Energy y/y	11-Dec-18	Nov	2.7%	2.6%
	JN	Core Machine Orders y/y	11-Dec-18	Oct	4.5%	-7.0%
	CH	Money Supply M2 y/y	11-Dec-18	Nov	8.0%	8.0%
WED	IN	CPI y/y	12-Dec-18	Nov	2.3%	3.4%
	US	CPI Ex Food and Energy y/y	12-Dec-18	Nov	2.2%	2.1%
THUR	EC	ECB Main Refinancing Rate	13-Dec-18	13-Dec	0.0%	0.0%
	BZ	Selic Rate	13-Dec-18	12-Dec	6.50%	6.50%
	TU	One-Week Repo Rate	13-Dec-18	13-Dec	24.00%	24.00%
FRI/SAT	CH	Retail Sales y/y	14-Dec-18	Nov	8.1%	8.6%
	CH	Fixed Assets Investment Ex-Rural YTD y/y	14-Dec-18	Nov	5.9%	5.7%
	CH	Industrial Production y/y	14-Dec-18	Nov	5.4%	5.9%

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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