Standard Chartered Private Bank

weekly market view

macro strategy | 30 November 2018

This reflects the views of the Wealth Management Group

Editorial

Stage set for a market rebound?

- **A less hawkish Fed and a likely truce in the US-China trade tussle could be the trigger for a rebound in risk assets, especially in the US and Asian stocks and bonds.**
- **Equities:** US energy sector could rebound sharply if OPEC and Russia agree to output cuts. Euro area stocks could come under further pressure if the US imposes a 25% tariff on auto imports.
- **Bonds:** Asian USD bonds remained resilient, while EM USD bonds were volatile amid Russia-Ukraine tensions, underscoring Asian USD bonds' relatively defensive characteristics.
- **FX:** The USD/CNH rally is showing signs of fatigue ahead of the Trump-Xi G20 meeting. Any break below 6.85 would confirm upward pressure has eased, paving way towards 6.78.

What's new?

- **Stage set for a market rebound?** Global equities rebounded, with US stocks recovering from a 10% correction, after Fed Chair Jerome Powell signalled that the central bank may slow the pace of its rate hikes. The comments put at ease one of the two major policy concerns that had weighed on equities, i.e. a continued rise in US interest rates and a resulting tightening of US and global liquidity conditions. Market expectations have eased to less than two 25bps Fed rate hikes in 2019, from close to three hikes anticipated in early October. The other risk, of a further escalation in US-China trade conflict, could dissipate if President Trump and President Xi reach a truce at the upcoming G20 summit. The easing of one or both policy risks would be a positive for US and Asia ex-Japan equities and Emerging Market (EM) bonds, in our view (see page 3 for more).
- **Stocks, USD testing key technical levels**. The S&P500 faces technical resistance at 2,815 (2.8% above current level). A break higher would set the next target at 2,940. The MSCI Asia ex-Japan is testing key resistance at the early-November high. A break higher would confirm that the downward pressure has eased, opening way toward the September high (8% above current level). A reversal in USD strength likely holds the key to an Asian equity market rebound. A break in the USD index below 96.50 would be a positive signal (see chart on right).
- **Euro area faces US auto tariff risk**. The European auto sector has been under pressure due to a sharp decline in demand for diesel cars and the cost of meeting new emission standards. An emerging negative catalyst is the possibility that President Trump slaps a 25% tariff on auto imports, excluding Canada and Mexico. Technically, Euro area equities found support at the bottom of the channel established in 2017. The upper end of the channel is 8% higher than current levels, a level which could be reached near term if sentiment improves or President Trump does not follow through with his import tariffs. The Euro area consumer discretionary sector, which includes autos, is one of our core holdings, as are Euro area equities.

What we are watching

- **OPEC-Russia meeting.** The 6 December summit could lead to output cuts, supporting oil prices and US energy sector equities.

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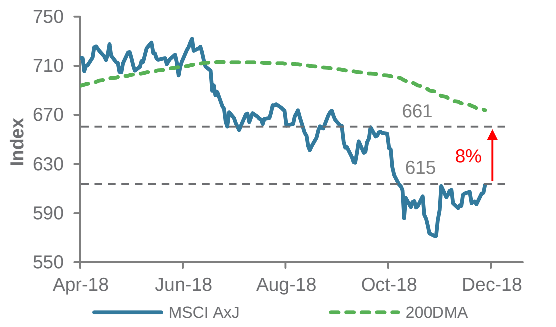
Any break in the MSCI Asia ex-Japan equity index above the November-high's resistance could potentially open the way for another 8% gain; the 200DMA remains a major barrier for any uptrend

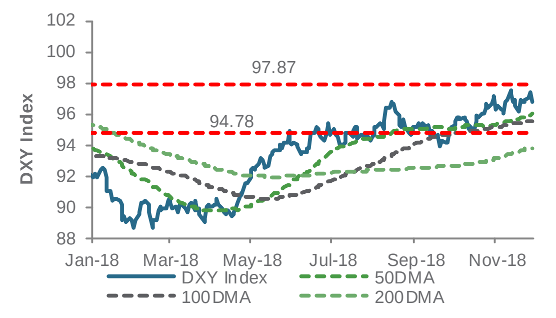
MSCI Asia ex-Japan index



Source: Bloomberg, Standard Chartered

A reversal in the USD's strength likely holds the key to a sustained Asian equity market rebound; a break below 96.50 could take the USD index towards 94.78

USD (DXY) index



Source: Refinitiv EIKON, Standard Chartered

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What does this mean for investors?

Global equities rebounded amid expectations of a slower pace of Fed rate hikes and a possible truce in US-China trade tensions. EM bonds recovered; crude oil extended losses.

Equities: US, Asia ex-Japan outlook improve

- **Hong Kong and China market sentiment improves.** Growing expectations that the US Fed could slow the pace of interest rate hikes in 2019 is positive for fund flows into the Asia ex-Japan region and the interest-rate-sensitive Hang Seng Index. We also see good technical support for both the Hang Seng Index and China A-shares. China's government has recently announced measures to encourage corporate share buybacks and mergers and acquisitions, besides supporting increased bank lending to private enterprises to ease liquidity concerns. MSCI China A-shares are trading at 12-month forward P/E ratio of 9.8x, which is below its long-term average. The China A-shares market is a preferred equity market in the Asia ex-Japan region.
- **The energy sector could get a boost from OPEC.** The S&P500 index rebounded from a support just above 2,600 amid easing concerns about Fed rate hikes. The energy sector is in focus ahead of the 6 December OPEC-Russia meeting in Vienna. The sector is one of the worst performers this quarter, reflecting the 34% peak-to-trough decline in US crude oil prices. We note that diversity in the market is extremely low, with a majority of investors positioned for weakness in the oil price. Oil prices and energy sector equities could see a sharp recovery if the OPEC meeting results in a proposal to reduce output. We prefer the Euro area energy sector. The US remains our preferred equity market globally.

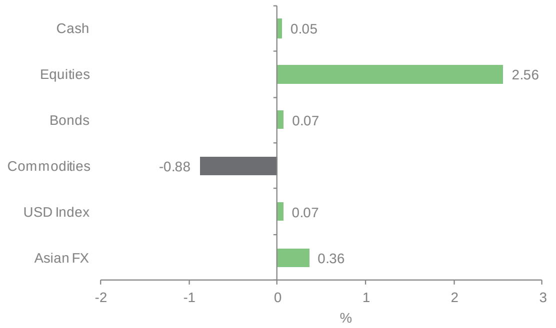
Bonds: US Treasury yields drop as Fed signals dovish turn

- **Fed comments drive Treasury yields lower**. US yields had already been under pressure from weak economic data and equity market weakness. Fed Chair Powell's dovish comments drove 10-year Treasury yields towards 3%, the lowest since September. Market expectations of around two rate hikes in 2019 aligns with our outlook and supports our view that the yield is likely to remain in the 3.00%-3.25% range in the next 12 months.
- **US High Yield bonds remained under pressure** as oil prices continued to decline, leading to higher yield premiums. While yield premiums have increased meaningfully since early October, we do not view the current sell-off as a buying opportunity given elevated valuations leave little buffer for any deterioration in credit quality, in our view.
- **Asia bonds remain resilient**. Emerging Market (EM) bonds remained volatile as USD strength initially hurt local currency bonds, while Russia-Ukraine tensions led to higher yield premiums for USD-denominated bonds. However, the bonds recovered subsequently as the USD stabilized. Asian USD bonds remained resilient, with yield premiums broadly unchanged. In recent weeks, Asian bonds have yet again demonstrated their value as a defensive allocation. We continue to view them as a core holding within a diversified allocation.

FX: USD/CNH rally showing signs of fatigue

- **USD/CNH holds above support ahead of Trump-Xi meeting.** The focus remains on the upcoming G20 meeting. Expectations of further monetary stimulus amid a slowing China economy are also providing support to the pair. On technical charts, any break below the 6.85 support could confirm that the upward pressure has eased, paving the way towards the August low of 6.78.

Benchmark (USD) performance w/w*



**Week of 22 November 2018 to 29 November 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 and Asia equity technicals have turned positive

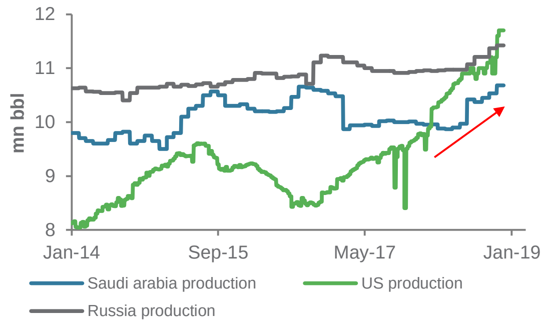
Technical levels of key market indicators as on 29 Nov

Index	Spot	1st support	1st resistance	Short-term trend
S&P500	2,738	2,680	2,773	↗
STOXX 50	3,174	3,126	3,200	↗
FTSE 100	7,039	6,939	7,158	↗
Nikkei 225	22,263	21,470	23,000	→
Shanghai Comp	2,567	2,450	2,690	↓
Hang Seng	26,451	25,500	27,300	↗
MSCI Asia ex-Japan	614	583	637	↗
MSCI EM	998	955	1,007	↗
Brent (ICE)	60	55	66	↓
Gold	1,224	1,196	1,240	↓
UST 10Y Yield	3.03	2.93	3.17	↘

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

Oil output has risen this year in the world's top three producers; any cutback in OPEC production would help to support oil prices and energy sector equities

Crude oil output in the US, Russia and Saudi Arabia



Source: Bloomberg, Standard Chartered

Market expectations of Fed rate hikes in 2019 have eased to less than two rate increases, from almost three hikes anticipated in early October

Market expectations of Fed rate hikes in 2019

Source: Bloomberg, Standard Chartered

Top client questions

Q1. What is our near-term outlook on Asia ex-Japan equity and bond markets?

Asian assets have sold off year-to-date amid reducing foreign inflows (following Fed interest rates hikes and a stronger USD) and often tightening domestic policy. China's deleveraging efforts and the escalation in US-China trade tensions further compounded the negative sentiment in the region. However, a recent softening of the Fed's stance, a possible easing of USD appreciation pressures and improving technicals for many regional markets signal the possibility of an improving near-term outlook for regional financial markets.

Weak sentiment may set the stage for a potential rebound

Equities: Earnings momentum in Asia has rolled over sharply since Q2 2018 and remains weak, weighed down by slower growth and weaker currencies. We expect consensus will likely continue to downgrade earnings estimates, **but the pace of deterioration will probably slow** as policy support from China and more benign rate hike expectation starts coming through.

While it is always difficult to time a precise market bottom, with the significant valuation de-rating, less bad news may potentially be a trigger for more positive market reactions. Additionally, stable fundamentals increasingly argue in favour of an improving **risk reward trade-off for Asia ex-Japan equities in the short term**.

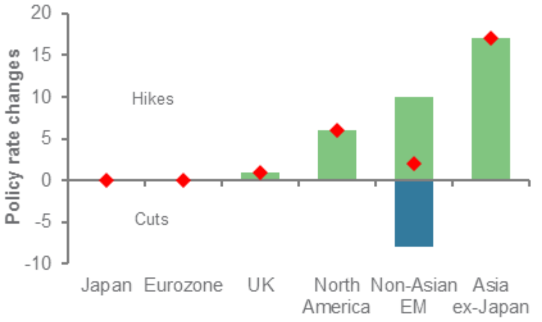
Technical: The MSCI Asia ex-Japan index is now testing key resistance at the early-November high of 615.10. Any break above this will confirm that downward pressure had eased, opening the way initially toward the September high of 661 (about 8% above current levels). It is too soon to say if the multi-month downtrend has ended – it remains possible that the potential short-term rebound is a pause rather than a reversal of the downtrend. In this regard, the 200-day moving average would be an important barrier to watch (now at about 675; about 10% from current levels).

Hang Seng: Within Asia, the Hang Seng index looks particularly interesting from a technical standpoint given the break above this week's trendline resistance of 26,220, which suggests the downward pressure has abated for now. The break has opened the way toward the September high of 28,000.

Bonds: Asian USD bonds have been under pressure over the past few months, as yield premiums have risen, largely driven by concerns around China. This has meant that yields on offer have become more attractive, especially in High Yield (HY) bonds. However, liquidity challenges onshore amid continued deleveraging efforts in China mean we continue to favour better-quality Investment Grade (IG) bonds over HY bonds. The yield on the Asian USD benchmark bond index is now at a reasonably attractive 5.4% level.

Asian central banks led policy tightening

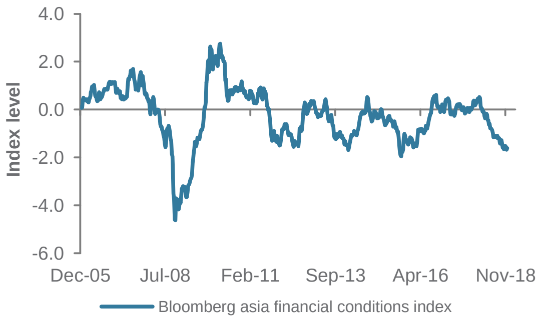
Number of times central banks hiked policy rates over the past 12 months



Source: Refinitiv EIKON, Standard Chartered

Asian financial conditions now the tightest since 1H 2015

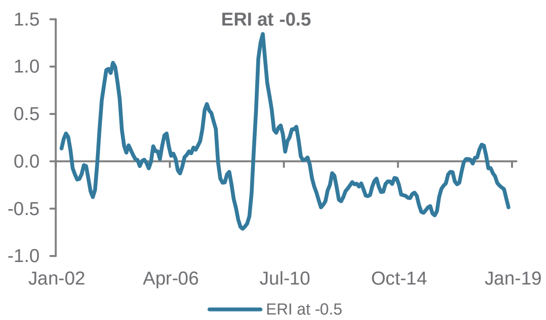
Bloomberg Asia ex-Japan Financial conditions index (which tracks the overall level of stress in Asia ex-Japan money, bond and equity markets to help assess the availability and cost of credit)



Source: Bloomberg, Standard Chartered

Earnings momentum have rolled over since Q2

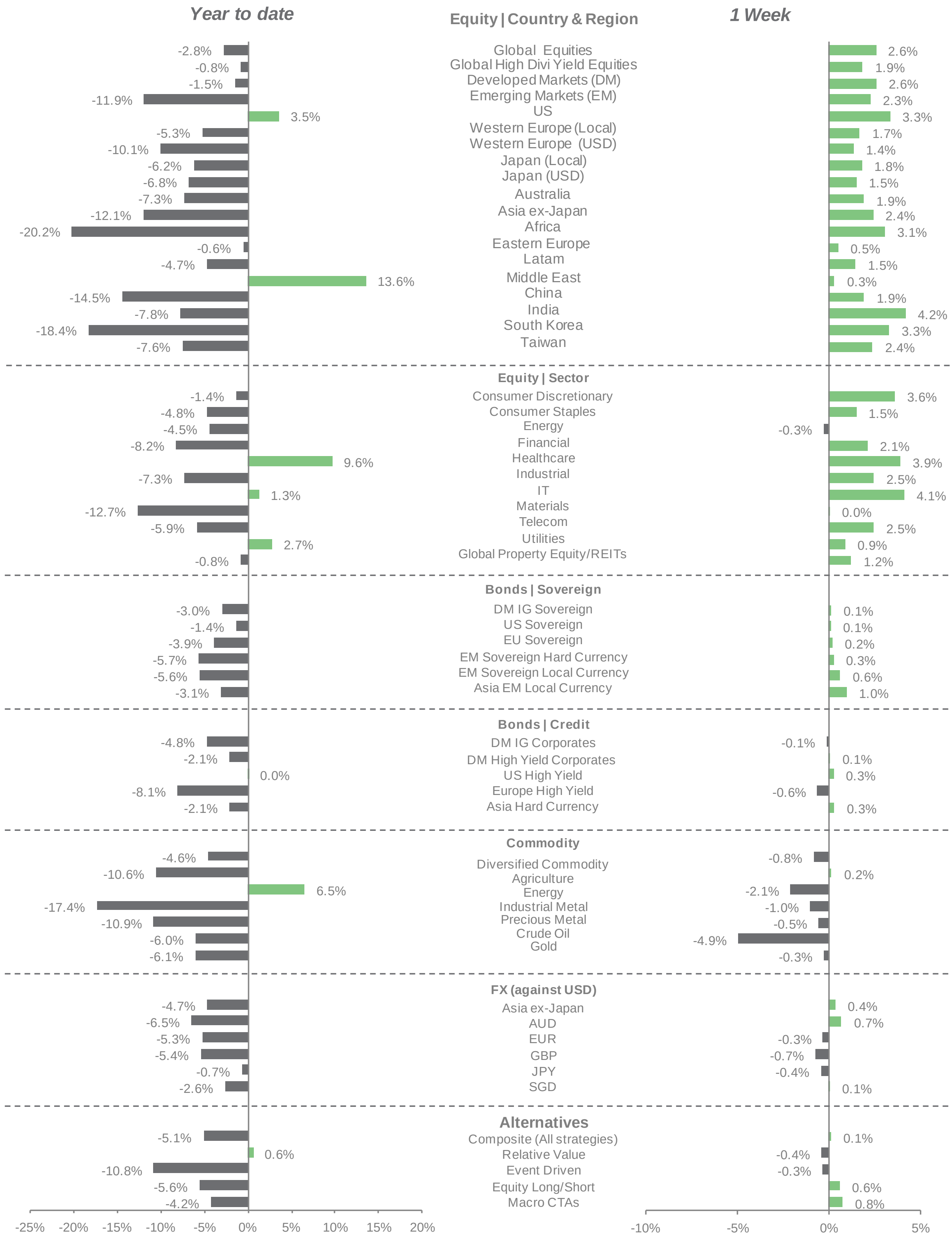
MSCI Asia ex-Japan earnings revision index (3MMA)



Source: Factset, Standard Chartered

Earnings revision refers to the upgrades relative to downgrades in consensus earnings estimates

Market performance summary*



**Performance in USD terms unless otherwise stated, YTD period from 31 December 2017 to 29 November 2018, 1 week period: 22 November 2018 to 29 November 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
MON	US	ISM Manufacturing	03-Dec-18	Nov	58.0	57.7
TUE	AU	RBA Cash Rate Target	04-Dec-18	4-Dec	1.5%	1.5%
	EC	PPI y/y	04-Dec-18	Oct	–	4.5%
WED	CH	Caixin China PMI Composite	05-Dec-18	Nov	–	50.5
	IN	RBI Repurchase Rate	05-Dec-18	5-Dec	6.5%	6.5%
	EC	Retail Sales y/y	05-Dec-18	Oct	–	0.8%
	US	ISM Non-Manufacturing Index	05-Dec-18	Nov	59.5	60.3
THUR	GE	Factory Orders WDA y/y	06-Dec-18	Oct	–	-2.2%
	US	Trade Balance	06-Dec-18	Oct	-$54.0b	-$54.0b
FRI/SAT	CH	Foreign Reserves	07-Dec-18	Nov	–	$3053.10b
	US	Average Hourly Earnings y/y	07-Dec-18	Nov	3.0%	3.1%
	US	Change in Nonfarm Payrolls	07-Dec-18	Nov	205k	250k
	US	Unemployment Rate	07-Dec-18	Nov	3.7%	3.7%
	US	U. of Mich. Sentiment	07-Dec-18	Dec P	97.0	97.5

	Event	This Week	Date	Period	Actual	Prior
MON	JN	Nikkei Japan PMI Mfg	26-Nov-18	Nov P	51.8	52.9
TUE	CH	Industrial Profits y/y	27-Nov-18	Oct	3.6%	4.1%
	JN	PPI Services y/y	27-Nov-18	Oct	1.3%	1.1%
	US	Conf. Board Consumer Confidence	27-Nov-18	Nov	135.7	137.9
WED	EC	M3 Money Supply y/y	28-Nov-18	Oct	3.9%	3.6%
	US	Core PCE q/q	28-Nov-18	3Q S	1.5%	1.6%
	US	GDP Annualized q/q	28-Nov-18	3Q S	3.5%	3.5%
THUR	EC	Economic Confidence	29-Nov-18	Nov	109.5	109.7
	GE	CPI EU Harmonized y/y	29-Nov-18	Nov P	2.2%	2.4%
	US	Personal Income	29-Nov-18	Oct	0.5%	0.2%
	US	Real Personal Spending	29-Nov-18	Oct	0.4%	0.1%
FRI/SAT	JN	Industrial Production y/y	30-Nov-18	Oct P		-2.5%
	CH	Manufacturing PMI	30-Nov-18	Nov	–	50.2
	EC	Unemployment Rate	30-Nov-18	Oct	–	8.1%
	US	Chicago Purchasing Manager	30-Nov-18	Nov		58.4

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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