Standard Chartered Private Bank

weekly **market view**

macro strategy | 18 January 2019

This reflects the views of the Wealth Management Group

Editorial

Tactically bullish on equities

- **We are tactically positive on equities for the next three months. China's coordinated policy support is likely to add fuel for a near-term rally in risk assets.**
- **Equities:** China's measures to boost consumption and speed up projects are positive for local equities. US Q4 18 earnings have surprised positively so far, supporting our bullish US equity view.
- **Bonds:** Emerging Market USD government bonds are likely to benefit from positive sentiment and renewed fund inflows.
- **FX:** The UK parliament's rejection of Premier May's Brexit plan reduces the chance of a 'hard' Brexit; this is positive for GBP/USD. 1.2700 is expected to be good support.

What's new?

- **Tactically bullish on equities.** We believe the c.10% rebound in global equities from December's two-year lows has more room to run. China's decisive shift in policy from 2018's deleveraging efforts offers support to our near-term view on risk assets. Beijing's plans of larger tax cuts, reduced financial burdens for small-and-medium companies, faster approval of infrastructure projects and increased local government bond issuance are likely to support growth. These measures, along with still-robust US economic activity (confirmed by the Fed's latest Beige Book survey), a significant easing of Fed rate hike expectations and signs of a thaw in Sino-American trade tensions, are likely to help support sentiment in the next 1-3 months. The MSCI All-Country World index is testing resistance at current levels. A break higher could open the way for another 5% gains.
- **Prefer 'Quality' in equities.** Within a diversified allocation, we believe 'Quality' stocks are likely to outperform 'Growth' or 'Value' stocks, both globally and in the US, over the next 12 months. This is because 'Quality' equities – characterised by high return-on-equity, low corporate leverage and low earnings variability – tend to perform well during times of elevated market volatility (which we envisage for 2019). The valuations of 'Quality' stocks have also become more attractive following the recent equity market correction.
- **GBP/USD gets a boost as 'hard' Brexit chances slump.** PM May's soft-Brexit plan was overwhelmingly voted down by the parliament (432 vs 202). Although May survived a subsequent no-confidence vote, we believe the rejection of her Brexit plan and an earlier vote, giving the parliament more say on the nature of a Brexit deal, reduces the prospects of the UK leaving the EU without a negotiated arrangement. It also raises the chances that the Brexit deadline may be pushed back beyond 29 March. Both these prospects are positive for the GBP. With GBP/USD facing near-term resistance c.1.3100, we would look to add exposure on any dip towards 1.2700. (See page 3 for details)

What we are watching

- **US government shutdown sets a record.** The ongoing month-long US government shutdown, the longest ever, remains a concern as every additional week is likely to cut US growth by around 0.1ppt per quarter, according to some estimates.

Contents

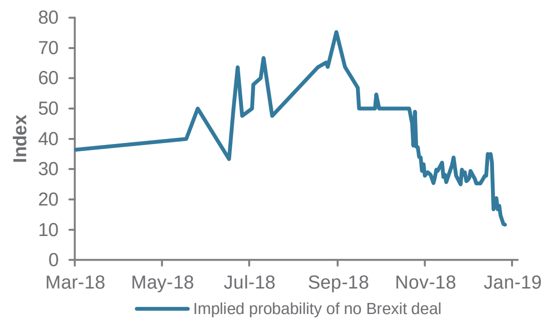
The probability of a Fed rate hike in Q1 2019 has plummeted after several Fed policymakers said they would be more patient in hiking rates

Market-based probability of a Fed rate hike in Q1 2019

Source: Bloomberg, Standard Chartered

The probability of a 'no-deal' (or 'hard') Brexit has declined significantly over the past few weeks after the UK parliament voted down PM May's proposals

Probability of a 'no-Brexit deal'



Source: Oddschecker, Bloomberg, Standard Chartered

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What does this mean for investors?

Global equities extended their rebound, led by US stocks, as risk sentiment continued to improve. US High Yield bonds continued to lead gains in debt markets. Oil pared back some of its gains.

Equities: US corporate earnings beat forecast

- **US Q4 18 earnings surprise positively.** Of the 10% of the S&P500 companies that have reported Q4 2018 earnings so far, 80% have surpassed expectations. US banks were the first to report, with most beating forecasts, although Q1 2019 earnings guidance has been cautious in light of expectations of a slower pace of Fed rate hikes going forward. The US remains our preferred equity market amid still-robust earnings (14% y/y growth expected for Q4 2018) and more attractive valuations following the recent pullback. Among the various US equity sectors, we prefer healthcare for its defensive nature and the energy sector, which is likely to benefit from an oil price rebound.
- **China measures to mitigate trade impact positive for equities.** While markets await developments in the US-China trade negotiations scheduled on 30-31 January, weaker-than-expected December economic data has lifted expectations of more stimulus measures. China's government bodies recently announced the need for more supportive measures, including larger tax cuts, with an aim to boost consumption, lower financial burdens for small- and medium-sized companies, speedier approvals for infrastructure projects and increased local government bond issuance. This follows earlier cuts in bank reserve requirements to boost lending. We expect the fiscal and monetary measures to support economic growth and corporate earnings, helping revive local equities whose valuations have fallen below historical averages. This supports our preference for China onshore, A-share equities within Asia ex-Japan.

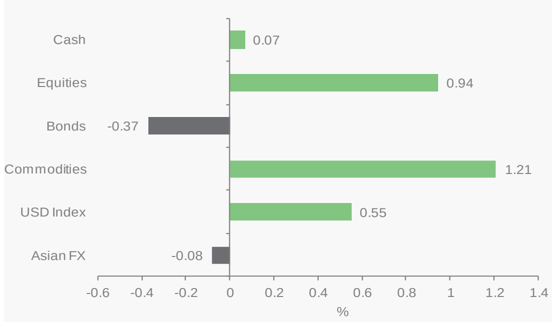
Bonds: US HY bond rally continues; opportunity to switch

- **Remain cautious on HY bonds.** US High Yield (HY) bonds continued to rally amid the recovery in global risk sentiment. Yield premiums have declined almost 100bps from the start of the year. We continue to remain cautious on the asset class as we enter the late stage of the business cycle and would use the current rally to trim exposure and switch to Emerging Market (EM) bonds.
- **Fund inflows support EM bonds.** EM USD government bonds rallied as they benefitted from the positive sentiment and fund inflows. Within EM, HY government bonds rallied more than Investment Grade (IG) bonds. We expect EM USD government bonds to remain supported by the positive sentiment and attractive valuations. Asian USD bonds remained steady despite the notable uptick in supply, especially from Chinese HY issuers. Although we continue to expect Asian USD bonds to remain less volatile than other EM bonds, yield premiums could increase if supply picks up further.

FX: Opportunities in silver, GBP/AUD

- **Looking to turn bullish on silver.** The link between silver and gold has reached an extreme level that is signalling a rebound in silver. In addition, physical demand for silver has started to increase. The next resistance is about 7% above current levels.
- **Opportunity in GBP/AUD.** The GBP is undervalued on a fair-value basis, while AUD appears under pressure with the rate cycle on hold and the market starting to price in rate cuts. Australia's economic remains clouded by persistent weakness in its housing market. We see a potential 3% upside in GBP/AUD.

Benchmark (USD) performance w/w*



**Week of 10 January 2019 to 17 January 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 equity market technicals remain positive

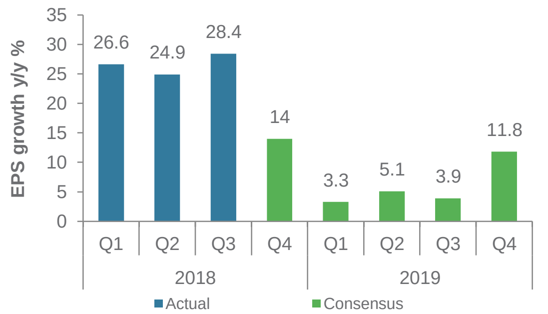
Technical levels of key market indicators as on 17 Jan.

Index	Spot	1st support	1st resistance	Short-term trend
S&P500	2,636	2,570	2,673	↗
STOXX 50	3,069	3,000	3,116	→
FTSE 100	6,835	6,730	7,002	→
Nikkei 225	20,606	19,700	20,960	↗
Shanghai Comp	2,560	2,490	2,600	↓
Hang Seng	26,756	25,650	28,000	↗
MSCI Asia ex-Japan	617	585	630	↗
MSCI EM	1,009	968	1,020	↗
Brent (ICE)	61	55	64	→
Gold	1,291	1,265	1,325	↗
UST 10Y Yield	2.75	2.52	2.82	↘

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

US Q4 2018 earnings growth is expected to slowdown from earlier part of the year, but to remain at a healthy level

S&P500 index consensus quarterly earnings estimates



Source: Refinitiv EIKON, Standard Chartered

EM USD government bonds have recently caught up with US HY bonds after 2018's underperformance

EM USD government bond and US HY bond total return indices (Index: 100 = 17 July 2018)

Source: Bloomberg, Standard Chartered

Top client questions

Q1. What is the likely outcome of the UK's Brexit process?

In our opinion, there are three possible outcomes of the process: a 'soft' Brexit (broadly along the lines of the deal negotiated with the EU), a 'no' Brexit and a 'hard' Brexit. We believe the last option is the least likely, although the path and timing to this being resolved is still unclear. We believe the first two outcomes would be positive for the GBP, which remains deeply undervalued.

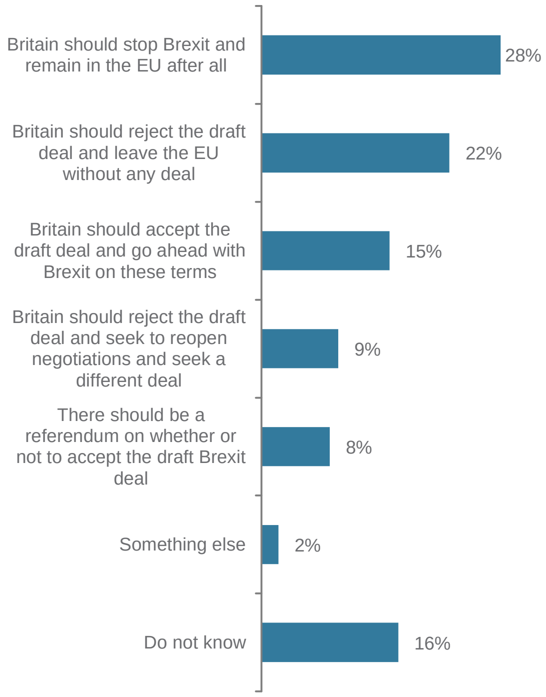
This past week saw PM May convincingly lose a parliamentary vote on the Brexit deal she negotiated with the EU before defeating a no-confidence motion tabled by Labour Party leader Corbyn. Both outcomes were largely expected, although the scale of the defeat on the Brexit deal was much larger than expected. This does not necessarily mean that the deal is dead in the water, but it does highlight the challenges in gaining a consensus, especially by the 29 March deadline when the UK is due to leave the EU.

Before the vote, PM May's stance was that it is this deal ('soft' Brexit) or no deal ('hard' Brexit) on 29 March. Now there is increasing speculation about requesting an extension to the 29 March deadline and/or calling another referendum, something that May is still resisting despite rising political pressure to reconsider. What looks highly unlikely at this stage is a major overhaul of the deal. Some tweaking of the deal is possible, but the EU does not appear willing to open even that option unless there is a strong indication that such a tweaking would be decisive in getting it through the parliament.

What to watch: PM May has opened discussions with opposition Members of Parliament in an attempt to get the necessary support for the Brexit deal that is on the table. This increased parliamentary involvement reduces the likelihood of a hard Brexit as this is the least favoured option by the vast majority of parliamentarians. Over 70 Labour Members of Parliament (besides all members from the Scottish National Party) are now supporting a second referendum, and this number is growing. As a result, Oddschecker is now quoting a 48% probability of a second referendum.

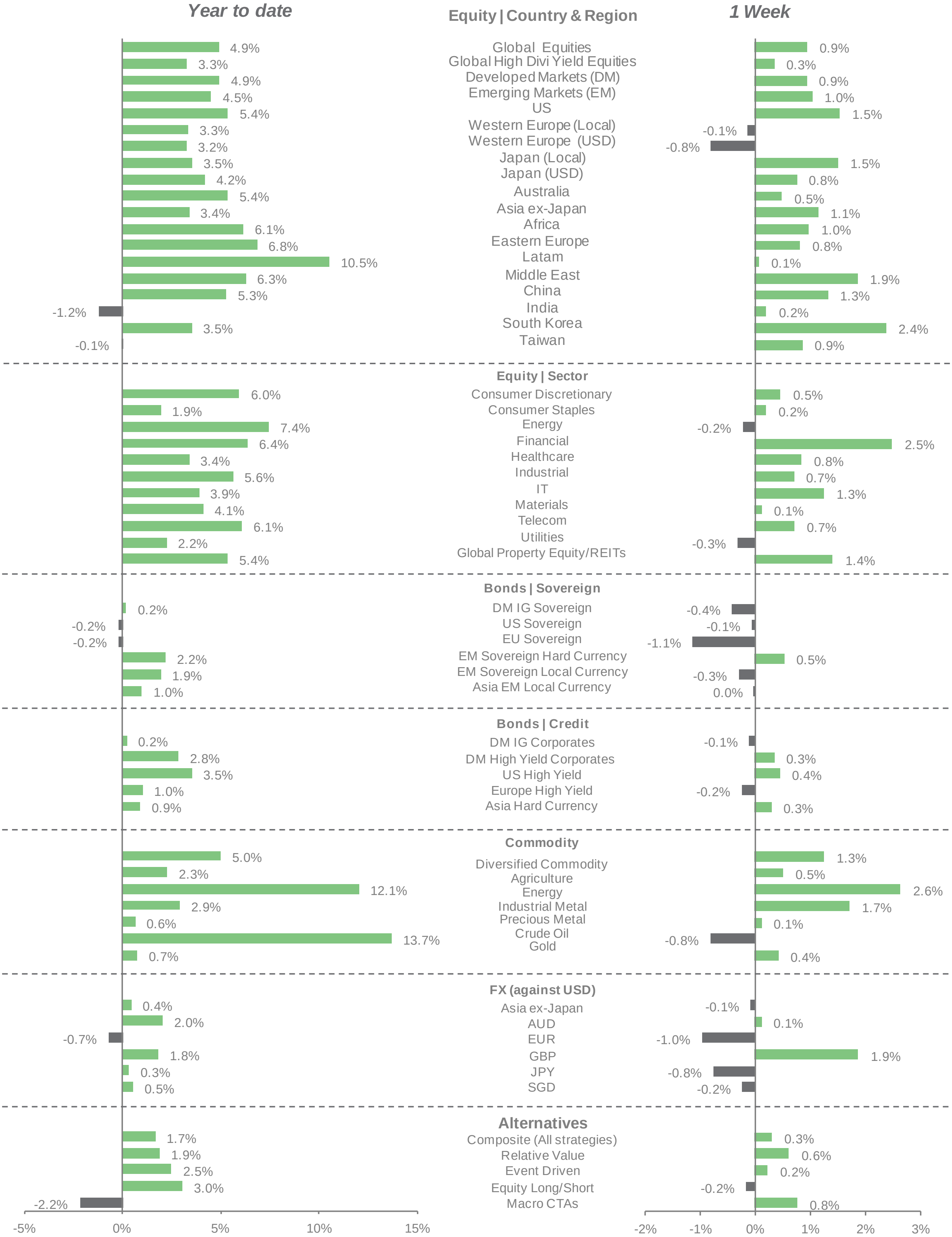
UK opinion polls show a 'no' Brexit is the most popular choice

YouGov poll results on various Brexit options



Source: YouGov, Standard Chartered

Market performance summary*



**Performance in USD terms unless otherwise stated, YTD period from 31 December 2018 to 17 January 2019, 1 week period: 10 January 2019 to 17 January 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	CH	Retail Sales y/y	21-Jan-19	Dec	8.2%	8.1%
	CH	Industrial Production y/y	21-Jan-19	Dec	5.3%	5.4%
	CH	Fixed Assets Ex Rural YTD y/y	21-Jan-19	Dec	6.0%	5.9%
	CH	GDP y/y	21-Jan-19	4Q	6.4%	6.5%
TUE	UK	Average Weekly Earnings 3m/y/y	22-Jan-19	Nov	–	3.3%
	US	Existing Home Sales	22-Jan-19	Dec	5.27m	5.32m
WED	JN	Exports y/y	23-Jan-19	Dec	–	0.1%
THUR	GE	Markit/BME Germany Composite PMI	24-Jan-19	Jan P	–	51.6
	EC	Markit Eurozone Manufacturing PMI	24-Jan-19	Jan P	–	51.4
	EC	Markit Eurozone Services PMI	24-Jan-19	Jan P	–	51.2
	EC	Markit Eurozone Composite PMI	24-Jan-19	Jan P	–	51.1
	US	Markit US Composite PMI	24-Jan-19	Jan P	–	54.4
	US	Leading Index	24-Jan-19	Dec	-0.1%	0.2%
FRI/SAT	US	Cap Goods Orders Nondef Ex Air	25-Jan-19	Dec P	–	–
	US	New Home Sales	25-Jan-19	Dec	–	–

	Event	This Week	Date	Period	Actual	Prior
MON	IN	CPI y/y	14-Jan-19	Dec	2.2%	2.3%
	CH	Exports y/y	14-Jan-19	Dec	-7.6%	2.9%
TUE	CH	Money Supply M2 y/y	15-Jan-19	Dec	8.1%	8.0%
	US	PPI Ex Food and Energy y/y	15-Jan-19	Dec	2.7%	2.7%
	IN	Exports y/y	15-Jan-19	Dec	0.3%	0.8%
WED	JN	Core Machine Orders y/y	16-Jan-19	Nov	0.8%	4.5%
	UK	CPI Core y/y	16-Jan-19	Dec	1.9%	1.8%
	US	Import Price Index y/y	16-Jan-19	Dec	-0.6%	0.5%
THUR	US	Philadelphia Fed Business Outlook	17-Jan-19	Jan	17.0	9.1
	US	Initial Jobless Claims	17-Jan-19	12 Jan	213k	216k
FRI/SAT	JN	Natl CPI Ex Fresh Food, Energy y/y	18-Jan-19	Dec	0.3%	0.3%
	UK	Retail Sales Ex Auto Fuel y/y	18-Jan-19	Dec	–	3.8%
	US	Industrial Production m/m	18-Jan-19	Dec	–	0.6%
	US	U. of Mich. Sentiment	18-Jan-19	Jan P	–	98.3

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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