Standard Chartered
Private Bank

# weekly **market view**

**macro** strategy | 19 October 2018

This reflects the views of the Wealth Management Group

## Editorial

# Taking a pause

- **US Treasury yields and oil prices paused following strong gains in September, helping stabilise equities and corporate bonds. However, technicals suggest equities could stay range-bound in the short term.**
- **Equities:** Q3 US earnings continue to progress well, supporting our preference for US equities. However, Asian equities face more challenging near-term technicals. See page 3 for more on what technical indicators are signalling at the moment.
- **Bonds:** Rally in EM local currency bonds offers an opportunity to rebalance towards EM USD bonds, in our view.
- **FX:** USD outlook remains range-bound. We expect gold to stay supported in this environment.

### What's new?

- **Risky assets stabilise. Technical indicators suggest rangebound equity markets short-term. Stay diversified.** A turn lower in US Treasury yields and oil prices from the top of our expected ranges (around 3.25% and USD 85/bbl, respectively) have helped equity and corporate bond markets stabilise. We believe continued strength in US earnings, a lack of new inflation risks and Fed minutes this week that supported a view of gradual rate hikes are all reasons to be constructive. This includes our preferred US equity sectors like technology and discretionary (see page 2 for more). However, short-term US equity market technicals remain less bullish. In addition, the rebound in Asian equities looks weaker than in Developed Markets' (DM). Recent volatility re-emphasises our view that while we believe equities should outperform cash and bonds over the next 6-12 months, equity exposure is best gained within a diversified and balanced investment allocation.
- **Europe faces further uncertainty from Italy's budget and Brexit worries.** Optimists argue that while Italian authorities are willing to "keep an open dialogue" with the EU on budget deficits, the EU has already indicated it would not easily give in to Italy's proposal for higher deficits. This could spark short-term market worries. On Brexit, a new proposal to extend the UK's Brexit transition period "beyond 2020" risks extending uncertainty, though this remains more a risk for the GBP and UK markets.
- **China, Hong Kong equities remain directionless.** The autos sector was under pressure as recent M&A activity opened the possibility of greater foreign competition for mainland auto producers. Utilities, with their relatively stable earnings, have outperformed the broader market over the past month. The focus remains on the CNY for near-term cues, especially as it inches closer to the psychologically important level of 7.00 against the USD amid continued trade tensions.

### What we are watching

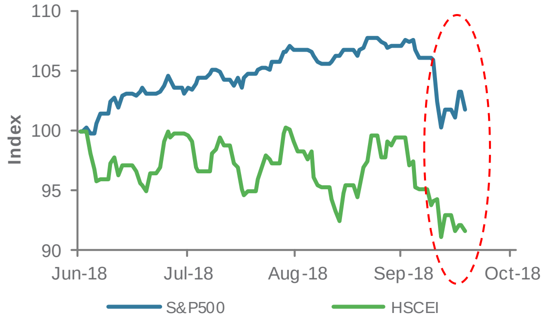
- **Focus on US politics, ECB in coming weeks.** With two weeks to go to US mid-terms, recent polls suggest Trump's Republican Party is increasingly likely to retain control of the Senate but not the House of Representatives. Any signals on interest rates at the ECB's meeting next week will also be key.

## Contents



**US equities have rebounded more strongly than many Asian equity markets after the recent sell-off**

*S&P500, HSCEI equity indices*




*Source: Bloomberg, Standard Chartered*

**Asian IG, HY bonds have similar performances YTD; we believe IG offers better returns for the risk taken**

*JACI IG and HY total return bond indices*


*Source: Bloomberg, Standard Chartered*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# What does this mean for investors?

**Global equities rebounded, led by the US and Emerging Markets, as oil and bond yields stabilised. The USD gained following the release of the Fed meeting minutes.**

## Equities: US earnings, seasonality support sector preferences

- **Early US earnings surprise positively.** Most of the companies that have reported Q3 earnings so far (48 out of 500) have reported upside surprises, with the largest aggregate surprise coming from the discretionary, financials and the new communication services sector. Meanwhile, staples is the only sector that reported more downside surprises than upside. We continue to prefer energy, financials, technology and consumer discretionary sectors in the US, noting the last two tend to do well in the November-April period.
- **China policy continues to walk a tightrope.** A rating agency's recent concerns over China's total government debt supports our view that authorities are unlikely to ease efforts to tackle excessive credit growth, suggesting the uptick in onshore corporate defaults is likely to continue. However, slowing economic growth suggests further, moderate measures to keep growth supported may yet be in the works. This balance of policies means we continue to prefer the defensive consumer staples and utilities sectors in China equities.
- **Non-Asia EM equities rebound.** In Brazil, polls showed a likely win by right-wing candidate Bolsonaro. Markets appear to have taken a more positive view of his more liberal economic agenda, though his ability to pass measures through Congress, even in the event of his eventual win, remains a risk.

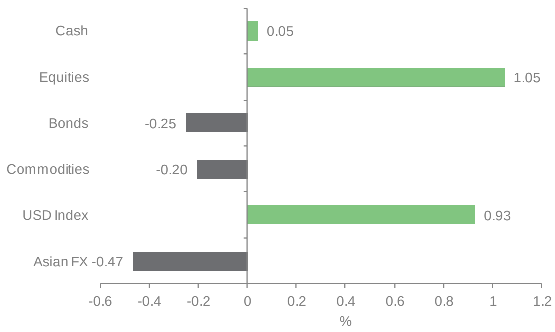
## Bonds: EM USD bonds remain preferred

- **Semblance of stability in government bonds.** US Treasury yields were range-bound after weeks of elevated volatility. The demand for safe-haven government bonds was likely helped by the equity market sell-off last week, which coincided with the reduction in the speculative short positioning in Treasuries. We continue to expect 10-year yields to remain capped at around 3.25% given elevated real (net-of-inflation) yields.
- **EM bonds rebound.** Emerging Market (EM) bonds delivered positive returns over the past week. Yield premiums over US Treasuries declined, but still remain relatively attractive, especially compared to DM HY bonds, in our view. EM local currency bonds delivered strong returns helped by gains in EM currencies and a rally in bond prices in Brazil, Turkey, India and South Africa. We favour using the rally in EM local currency bonds to rebalance into EM USD bonds, which remain our most preferred bonds sub-asset class.

## FX: Favour precious metals

- **USD/CNH testing key resistance.** USD/CNH is testing key resistance (the August peak at 6.9584), despite the USD index's break higher following the release of Fed minutes. A break higher towards 7.00 remains a key risk, especially given the risk of contagion to other asset classes. The US Treasury's semi-annual report refrained from labelling China a currency manipulator, though the report itself had a significant focus on the CNY.
- **Positive precious metals in the short term.** We continue to see a positive short-term outlook for gold. Technicals argue the break of USD 1,210/oz should open the way to USD 1,250/oz. We also see gold (and potentially silver, at a more attractive entry point) fitting well in a more balanced, diversified allocation. See the *Daily FX Navigator* for details.

### Benchmark (USD) performance w/w*




**Week of 11 October 2018 to 18 October 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)*

### S&P500 trend intact thus far

*Technical levels of key market indicators as on 18 Oct.*

| Index | Spot | 1st support | 1st resistance | Short-term trend |
|---|---|---|---|---|
| S&P500 | 2,769 | 2,745 | 2,819 | ↗ |
| STOXX 50 | 3,212 | 3,180 | 3,272 | ↘ |
| FTSE 100 | 7,027 | 6,865 | 7,220 | ↘ |
| Nikkei 225 | 22,229 | 22,270 | 23,050 | ↘ |
| Shanghai Comp | 2,486 | 2,380 | 2,665 | ↘ |
| Hang Seng | 25,455 | 24,200 | 26,850 | ↓ |
| MSCI Asia ex-Japan | 594 | 583 | 628 | ↓ |
| MSCI EM | 971 | 950 | 1,015 | ↓ |
| Brent (ICE) | 80 | 78 | 87 | ↑ |
| Gold | 1,227 | 1,180 | 1,240 | ↑ |
| UST 10Y Yield | 3.17 | 3.02 | 3.27 | ↗ |

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

### EM USD bonds remain one of our most preferred areas within bonds

*EM equities (MSCI EM Index), EM USD sovereign bonds (JPMorgan EMBI GD), EM local currency bonds (JPMorgan GBI-EM Local Index)*


*Source: Bloomberg, Standard Chartered*

### Precious metals likely to rebound in the short term

*Gold, Silver*


*Source: Bloomberg, Standard Chartered*

## Top client questions

**Q1. What can technical indicators tell us about whether last week's US equity market fall is a pause or a reversal of the uptrend?**

While the price action is still unfolding, currently we see technical indicators and charts illustrating a pause, rather than a reversal, of the long-standing uptrend in US equities.

**The big picture (longer-term charts)**

Even before last week's fall, the S&P500 index was showing signs of fatigue on longer-term charts. The failure to decisively break above the January high, coupled with a negative signal from momentum indicators, was a sign of loss of steam. We noted in last week's *Weekly Market View* that potential catalysts for and context behind the fall included US Treasury yields hitting multi-year highs, ongoing US-China trade tensions, geopolitical concerns (Italy, Brexit) and negative earnings revisions before the start of the US earnings season. In general, this combination of indicators does not necessarily imply a reversal. It needs to be validated by some sort of break of key support levels.

The index has not broken any previous supports. This includes the end-June low (at 2,692), which is a moderate one. A stronger support is the February low (2,532), which is well below current levels. In addition, the index is holding above the 200-day moving average (now at 2,767) and an uptrend line from end-2016. Granted the price action is still unfolding, but the absence of a follow-through price action this week – the index has not made a lower low this week compared with last week – is an important sign.

**The short-term picture**

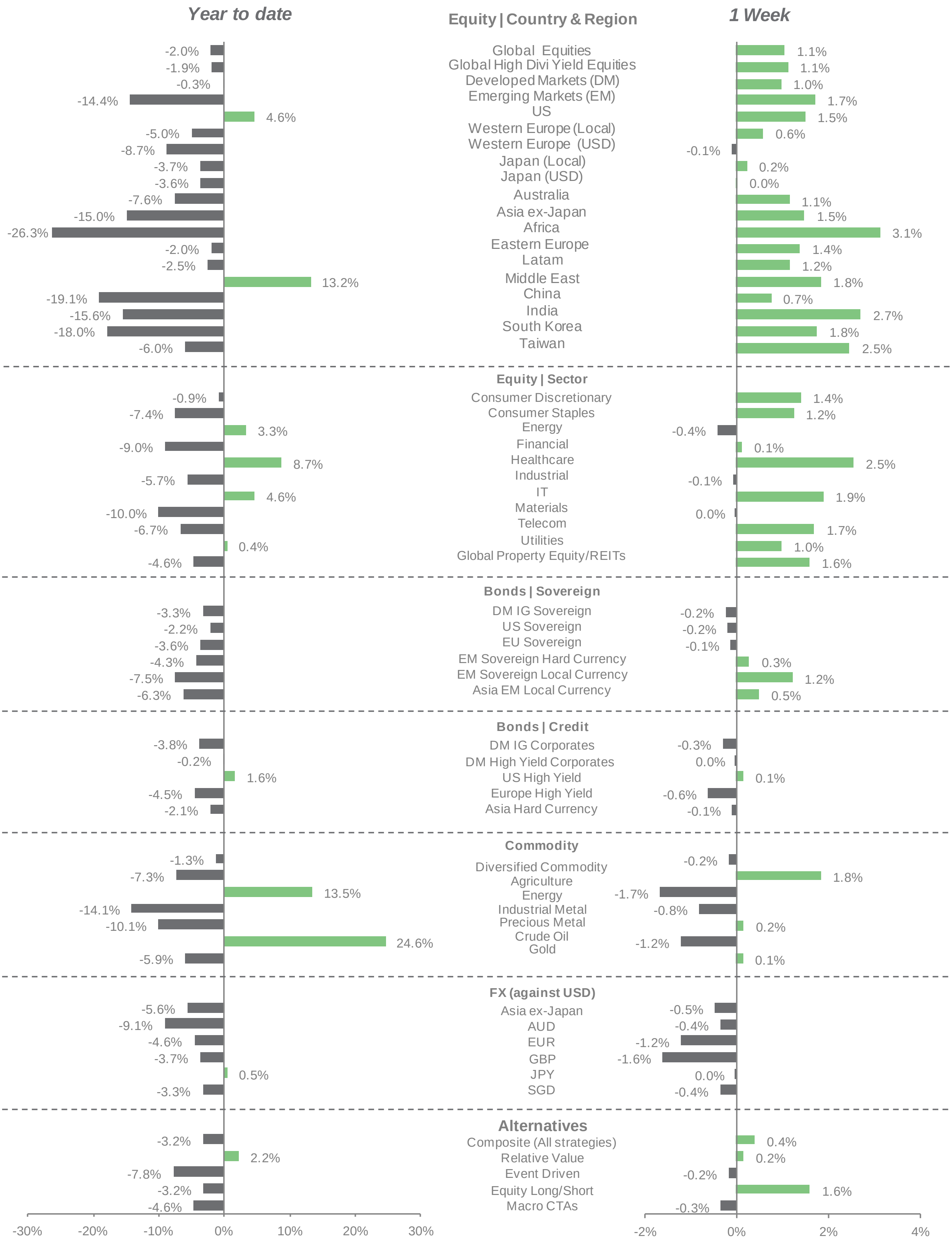
The index's break last week below a rising channel from Q2 (indicated on the chart by the two red dotted lines) is a confirmation that the upward pressure has faded in the short term. Moreover, this week's rebound looks feeble, raising the prospect of a retest of last week's low. Therefore, in the short term, it is possible that the index could spend some time in a sideways range. Having said that, when placed against the long-term picture discussed above, we still believe equities will perform positively provided the February low holds.

**We see a pause, rather than a reversal, in the S&P500's long-term uptrend**

*S&P500 index*


*Source: Bloomberg, Standard Chartered*

# Market performance summary*




**Performance in USD terms unless otherwise stated, YTD period from 31 December 2017 to 18 October 2018, 1 week period: 11 October 2018 to 18 October 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 | Chicago Fed activity index | 22-Oct-18 | Sep | – | 0.18 |
| TUE | SI | CPI y/y | 23-Oct-18 | Sep | – | 0.7% |
| | ID | Bank Indonesia policy rate | 23-Oct-18 | Oct | – | 5.8% |
| WED | US | New home sales | 24-Oct-18 | Sep | 628k | 629k |
| THUR | US | Fed Beige Book | 25-Oct-18 | – | – | – |
| | US | Durable goods orders | 25-Oct-18 | Sep P | -0.8% | 4.4% |
| | EU | ECB main refinancing rate | 25-Oct-18 | Oct | – | 0.3% |
| FRI/SAT | US | GDP q/q Annualized | 26-Oct-18 | Q3 A | 3.2% | 4.2% |
| | US | U. of Mich. Sentiment | 26-Oct-18 | Oct F | 98.6 | 99.0 |
| | JN | Tokyo CPI ex-Fresh food | 26-Oct-18 | Oct F | 1.0% | 1.0% |

| | Event | This Week | Date | Period | Actual | Prior |
|---|---|---|---|---|---|---|
| MON | US | Retail Sales Ex Auto and Gas | 15-Oct-18 | Sep | 0.0% | 0.2% |
| TUE | CH | CPI y/y | 16-Oct-18 | Sep | 2.5% | 2.3% |
| | UK | ILO Unemployment Rate 3Mths | 16-Oct-18 | Aug | 4.0% | 4.0% |
| | EC | ZEW Survey Expectations | 16-Oct-18 | Oct | -19.4 | -7.2 |
| | US | Industrial Production m/m | 16-Oct-18 | Sep | 0.3% | 0.4% |
| WED | UK | CPI Core y/y | 17-Oct-18 | Sep | 1.9% | 2.1% |
| | US | Housing Starts | 17-Oct-18 | Sep | 1201k | 1282k |
| | US | Building Permits | 17-Oct-18 | Sep | 1241k | 1249k |
| THUR | JN | Exports y/y | 18-Oct-18 | Sep | -1.2% | 6.6% |
| | UK | Retail Sales Ex Auto Fuel y/y | 18-Oct-18 | Sep | – | 3.5% |
| | SK | BoK 7-Day Repo Rate | 18-Oct-18 | 18-Oct | 1.5% | 1.5% |
| FRI/SAT | JN | Natl CPI Ex Fresh Food, Energy y/y | 19-Oct-18 | Sep | – | 0.4% |
| | CH | GDP y/y | 19-Oct-18 | 3Q | – | 6.7% |
| | CH | Retail Sales y/y | 19-Oct-18 | Sep | – | 9.0% |
| | CH | Industrial Production y/y | 19-Oct-18 | Sep | – | 6.1% |
| | CH | Fixed Assets Ex Rural YTD y/y | 19-Oct-18 | Sep | – | 5.3% |
| | US | Existing Home Sales | 19-Oct-18 | Sep | – | 5.34m |

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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