Standard Chartered Private Bank

Weekly Market View

The return of reflation?

Latest central bank growth forecast upgrades suggest the pandemic-led downturn is likely to be less severe than previously expected. This is likely to lend fundamental support to the liquidity-driven risk asset rally. We would use any pullback to add exposure to risk assets.

Equities: China's consumer discretionary sector offers an attractive opportunity to gain exposure to the recovery in consumption

Bonds: We remain positive on Asia High Yield USD bonds due to their still-cheap valuations and our constructive view on China's economic recovery

FX: We expect more short-term USD gains ahead of the US elections; however, we expect EUR/USD to hold above 1.1490 technical support level

Also find out...

Are M&As a new catalyst for US equities?

Is there more downside in the US technology sector?

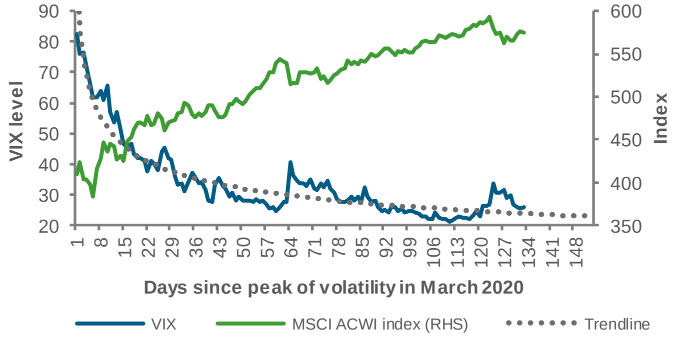
Will US equity market volatility decline further?

This commentary reflects the views of the Wealth Management Group of Standard Chartered Bank. Important disclosures can be found in the Disclosures Appendix.

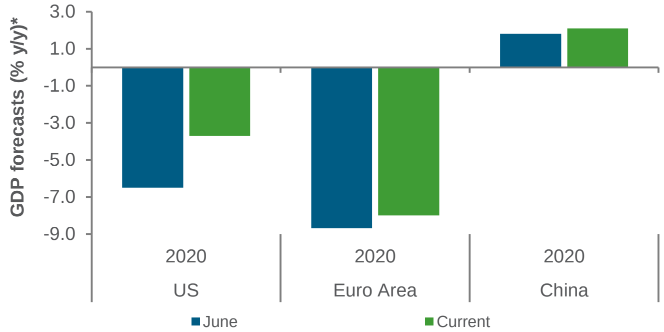
Charts of the week: Not as bad as feared

VIX, the market's "fear gauge", has continued to decline as the global downturn is turning out to be less severe than initially expected

Global stocks (MSCI All-Country World Index) have set new record highs in recent weeks, while S&P500's implied volatility index (VIX) fell



US, Euro area and China 2020 GDP forecasts* have been revised higher since June as concerns about the pandemic eased



Source: Fed, ECB, Bloomberg, Standard Chartered; US and Euro area growth forecasts are based on Fed & ECB estimates, China forecasts are consensus estimates

Editorial

The return of reflation?

September marks six months since global risk assets plunged as the World Health Organisation declared a global pandemic was underway. We have come very far since then, the change in outlook best captured by the S&P500 index's 'fear gauge' (the VIX implied volatility index). This index has plummeted from its March highs as fears of the pandemic and its economic impact eased, aided by unprecedented global fiscal and monetary stimulus and positive surprises in vaccine development. Have investors become too complacent, or is global reflation taking hold, providing fundamental support to the liquidity-driven rally?

We believe the global economic and corporate earnings downturn is likely to be less severe than initially expected. New forecasts from the Fed and ECB and continued improvement in China data in recent weeks support our view (see pages 3 & 4). The Fed this week revised its US GDP forecast for 2020 to a -3.5% contraction vs -6.5% forecast in June, with a 4.0% growth rebound forecast for 2021. Moreover, as anticipated, the Fed projected keeping interest rates close to 0% until at least 2023 as it switched its focus to maximising employment, downplaying inflation risks. The ECB and China policymakers have made similar supportive statements this month, standing ready to provide more stimulus.

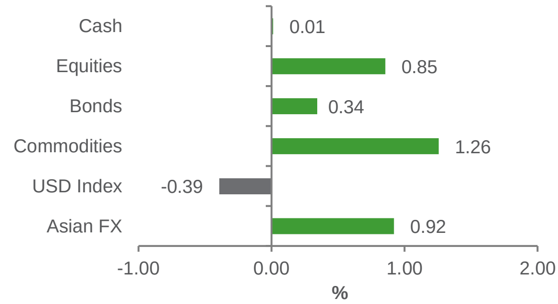
Governments will likely need to do more. EU members, after previously agreeing on an unprecedented plan to share the debt burden of a joint EUR 750bn spending package, have approved national stimulus plans, extending special unemployment support into next year. More stimulus is likely if the ongoing second COVID-19 wave extends into Q4 20.

The next focus is a potential fiscal package from the US Congress before it goes into recess ahead of the November election. We believe a deal will be agreed as no party wants to go into the election having let down voters amid still-high unemployment. The post-election scenario is more constructive as we believe both candidates have a pro-growth policy agenda, with Biden's USD 2trn "green" infrastructure plan standing out (see our *Emerging Theme* report on US elections for more details).

The above means we remain constructive on risk assets over the next 6-12 months and see any near-term setback to the rally due to upcoming event risks (see pages 4-6) as an opportunity to add exposure.

Equities, bonds and commodities rose in the past week, recovering from the previous week's losses; USD fell

Benchmark market performance w/w*



Source: Bloomberg; *week of 10 Sept. 2020 to 17 Sept. 2020

Our proprietary market diversity indicators point to low risk of a short-term trend reversal, except for the CNH

Market diversity across key asset classes

Level 1	Diversity	Diversity trend since 17-Aug-20	Fractal Dimension
Global Bonds	◐	↑	1.27
MSCI ACWI	◐	↑	1.39
Gold	◐	→	1.32
Equity			
MSCI US	◐	→	1.43
MSCI Europe	●	↑	1.82
MSCI AC AXJ	◐	→	1.33
Fixed Income			
DM Corp Bond	◐	↑	1.29
DM High Yield	◐	→	1.34
EM USD	◐	↑	1.35
EM Local Currency	◐	→	1.44
Asia Hard Currency	◐	→	1.30
Currencies			
USD/CNH	○	↓	1.25
EUR/USD	◐	→	1.31
USD/JPY	●	↓	1.53
GBP/USD	◐	↑	1.46
AUD/USD	◐	→	1.31

Source: Bloomberg, Standard Chartered; **Fractal dimensions below 1.25 indicate extremely low market diversity**

Legend: ○ Very low ◐ Low ● Moderate/high

The weekly macro balance sheet

	Positive for risk assets	Negative for risk assets
COVID-19	• Daily new cases in the US, Japan, Australia, Brazil and Mexico have come off their July/August highs, although a recent revival in the US needs to be watched closely • UK firm AstraZeneca resumed UK vaccine trials after a pause due to an adverse reaction in a participant • China inoculated tens of thousands of citizens in a trial	• Daily new cases continued to rise in Europe; Spain and France hit new record highs; India's total cases crossed 5m and daily cases hit a new high • A top US official said vaccines are unlikely to be widely available before mid-2021
	Our assessment: Neutral as the broad-based downtrend of US cases since July and continued rise in Europe follow recent trends.	
Macro data	• Fed upgraded US 2020 growth forecast to a -3.5% contraction vs -6.5% forecast earlier • US continuing jobless claims fell below expectations • Euro area economic sentiment (ZEW) rose in September to its strongest since 2004; industrial output in July beat forecast • China's credit growth rose more than expected in August • China retail sales, manufacturing investment posted their first gains since the pandemic outbreak, beating forecasts; industrial output growth beat estimates • Japan's exports fell less than expected in August; industrial output beat forecast in July	• US retail sales and industrial production rose less than expected in August; growth slowed from July • US housing starts and building permits fell below expectations in August • US budget deficit rose to a record USD 3tn in the first 11 months of fiscal 2020, more than double the full-year record set in 2009 • Euro area core inflation fell to a record low of 0.4% in August; exports fell y/y for the 5th straight month in July • German Economy Ministry said growth recovery "has recently weakened"
	Our assessment: Neutral, on balance, as stronger-than-expected Euro area economic sentiment, US job market, China data offset surprisingly weak US retail sales and Euro area inflation.	
Policy developments	• Fed pledged to keep benchmark rate close to 0%, at least till 2023 • US Speaker Pelosi said Congress should stay in session till lawmakers and the White House agree on a stimulus package • ECB's Lane and BoJ policymakers said they were ready to ease policy further to ensure inflation, which remains muted, reaches 2% target	• BoE said it was exploring negative rates to counter growing risks to the labour market • ECB's Weidmann said the Euro area economy is unlikely to regain its pre-crisis level until mid-2022
	Our assessment: Positive, on balance, amid the Fed's assurance of low rates and Pelosi's push for a fiscal stimulus package.	
Other developments	• Italy said the EU should not pull out of trade talks with the UK as "it is in everyone's interest to reach an accord" • Japan's Chief Cabinet Secretary Suga was elected Japan's next PM, succeeding Abe	• Oracle's bid for Tiktok remains incomplete amid US administration's concerns about national security • ECB's Makhlouf said it was "wise" to assume that the UK and EU will fail to reach deal
	Our assessment: US-China tensions and Brexit talks remain risks.	

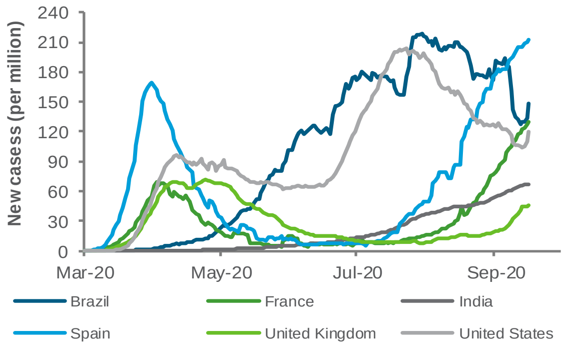
Our weekly net assessment: On balance, this week's data and policy were positive. Delay in finalising a new US fiscal package is a key risk.

(+) factor: Supportive central banks, strong EU sentiment, China data

(-) factor: Europe COVID rise, US-China tension, Brexit uncertainty

New COVID-19 cases continued to set new record highs in parts of Europe and in India; the revival in the US and Brazil need to be closely watched

Daily new COVID-19 cases per million people in the US, key European markets, India and Brazil



Source: Our World in Data, Standard Chartered

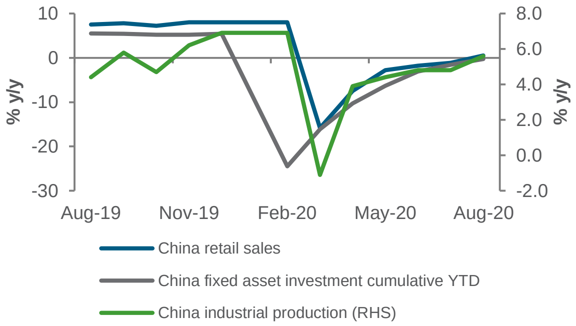
Euro area economic sentiment rose to its strongest level since 2004, but the second pandemic wave, if sustained into Q4 20, raises the risk of more economic restrictions

ZEW survey index of Euro area economic sentiment

Source: Bloomberg, Standard Chartered

China's retail sales, fixed asset investment and industrial production beat forecasts in August, underlining the continuation of the economic recovery that started in Q2

China retail sales, fixed asset investment (YTD) and industrial production annual growth



Source: Bloomberg, Standard Chartered

Top client questions

Are M&As a new catalyst for US equities?

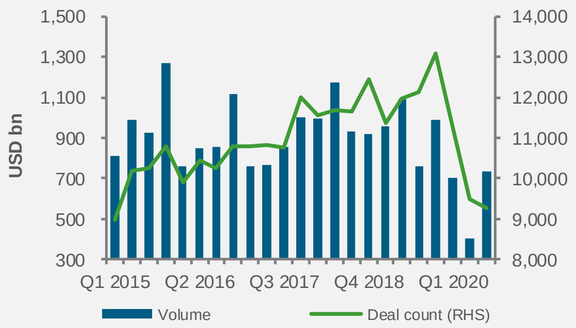
M&A activity has been severely impacted by COVID-19 this year, which is understandable as the global economic outlook is clouded and lockdowns obstruct negotiations and the conduct of due diligence. However, following a multi-year low in Q2 20, the M&A volume in dollar terms in Q3 20 so far has rebounded and exceeded Q1 20 levels already. Having said that, Q3 20 still has a very low deal count, as seen in the chart on the right. This implies there have been fewer, but much larger, transactions announced in Q3 20 so far.

M&A activity in the years prior to 2020 has been generally range-bound in volume, though the number of deals has been on a rising trend. This suggests that the rising equity markets we have seen in the last few years up to 2020 is more correlated to deal count, as opposed to deal volume in dollar amounts. M&A deal count is fuelled by broad optimism in corporate confidence and bustling economic activities, which are factors consistent with stronger equity markets.

As we have only seen large M&A transactions in Q3 20 so far but not a pick-up in deal count, this suggests broader corporate confidence and activities remain subdued. Consolidation in specific sectors would boost localised sector returns if the expected profit pool grows or it provides greater clarity on the sector outlook. However, the M&A deal count does not suggest broad strength for US equities. The technical picture for the US tech sector still looks weak in the short term, which would drag on the performance of US equities in the short-term. However, we remain positive in US equities on a 6-12m view given strong policy stimulus and the expected earnings recovery in 2021.

US M&A volume in USD terms has rebounded in Q3, but deal count has declined, suggesting the preponderance of a few large-size deals

US quarterly M&A volume in USD and number of deals



Source: Bloomberg, Standard Chartered

How can we play the recovery in China?

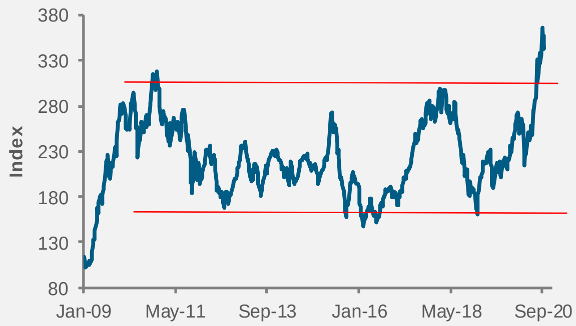
Consumption activity in China has rebounded amid a successful containment of COVID-19. Retail sales rose 0.5% y/y in August – the first increase for the year so far. Acceleration in service activities also pushed the non-manufacturing PMI to its highest level since early 2018.

We believe the gradual normalisation of activities could accelerate the consumption recovery trend in the upcoming National Day Golden Week (extended to eight days from the previous seven). According to Qunar, a Chinese online travel agency, air ticket booking volume has exceeded 90% of the same period last year. Domestic hotel bookings also witnessed a year-on-year increase in both room rates and room nights. Meanwhile, the Chinese government's new economic strategy of "internal circulation", focusing on domestic economy and reducing reliance on exports, is constructive for domestic consumption growth, in our view. While consumer staples have been resilient during the pandemic, we believe consumer discretionary is best positioned to benefit from the post-COVID recovery, especially higher quality services. According to Trip.com, 80% of hotel bookings for the Golden Week is for high-end hotels (4- and 5-star).

From a technical perspective, a breakout in the MSCI China Consumer Discretionary index reaffirmed an accelerating technical trend for the sector. China equities remain a preferred market in Asia ex-Japan, with consumer discretionary a preferred sector.

The technical breakout in China's consumer discretionary sector is supported by the fundamental rebound in consumer activity and services

MSCI China consumer discretionary sector index



Source: MSCI, FactSet, Standard Chartered

S&P500 index has support 0.7% below current level

Technical indicators for key markets as on 17 Sep. 2020

Index	Spot	1st support	1st resistance
S&P500	3,357	3,332	3,392
STOXX 50	3,317	3,309	3,332
FTSE 100	6,050	6,016	6,095
Nikkei 225	23,319	23,239	23,479
Shanghai Comp	3,270	3,255	3,291
Hang Seng	24,341	24,210	24,602
MSCI Asia ex-Japan	724	716	732
MSCI EM	1,107	1,093	1,119
Brent (ICE)	43.3	40.8	44.5
Gold	1,947	1,939	1,957
UST 10Y Yield	0.69	0.67	0.70

Source: Bloomberg, Standard Chartered

Top client questions (cont'd)

Is there more downside in the US technology sector?

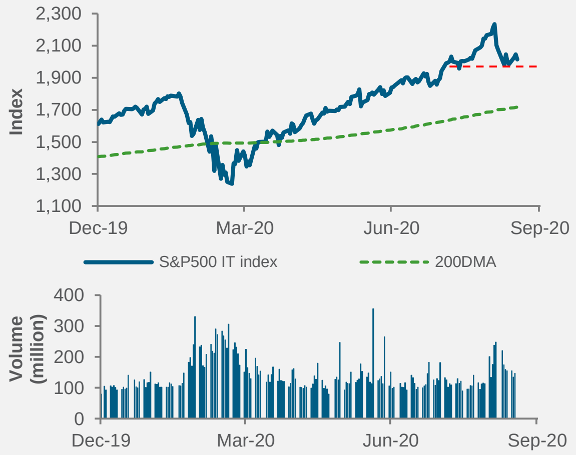
Yes, based on our technical assessment. We believe the pause in the S&P500 Information Technology sector's rally could extend a little further in the short term. However, we do not expect a change in the broader uptrend.

A negative divergence (higher high on the index associated with a lower high in momentum) between the index and the 14-week Relative Strength Index (RSI) on the weekly charts at its record high hit earlier this month indicates that the multi-month rally is losing steam. In addition, our market diversity indicator hit 1.288 on 1 September, suggesting low diversity (and very high optimism). Back-testing has revealed that the indicator dropping below the threshold of 1.250 has been associated with a consolidation/reversal in the index's trend.

The index is now testing key support at the mid-August low of 1954. Any break below could confirm that the upward pressure had faded in the short term. Higher volume on the declines and shallow rallies in recent days are a reflection of rejection of higher levels, suggesting the index may need to drop further to entice buyers. Any break below 1954 could pave way toward the 200-day moving average (now at 1,720; 14% below Thursday's close). We expect strong support to emerge around the 200-day moving average.

We believe the pause in the US technology sector could extend in the near term, although a change in the broader uptrend is unlikely unless the index falls below support

US S&P500 information technology index and trade volumes



Source: Bloomberg, Standard Chartered

Do you have any sector or quality preferences within Asia USD bonds?

Within Asia USD bonds, we have a preference for High Yield (HY) over Investment Grade (IG). While Asian IG bonds benefit from high quality, the high exposure to Chinese state-owned companies does expose the segment to US-China tension risks. On the other hand, HY bonds' relatively cheap valuations and our view of a gradual economic recovery should help bond prices increase (yield premiums decline) at a faster pace than IG bonds.

The positive view for HY bonds is also partly due to its high exposure to China's real estate sector, where developers are reporting higher YTD sales versus 2019. While recent proposals to impose property cooling measures and limits on the amount of debt companies can issue may lead to near-term consolidation, we view these developments as positive in the medium term.

More broadly, Asian USD bonds remain a preferred bond asset class as we like the high credit quality, low volatility and high exposure to China, which is probably the furthest along the path to economic recovery from the pandemic-related shock. Within this, we remain comfortable with higher-than-average exposure to Asian HY bonds.

We remain positive on Asia High Yield USD bonds due to their still-cheap valuations vs. Investment Grade peers and our constructive view on China's economic recovery

Yield differential between Asia High Yield USD and Asia Investment Grade USD bonds

Source: Bloomberg, Standard Chartered

Top client questions (cont'd)

Does the Fed meeting impact your USD outlook?

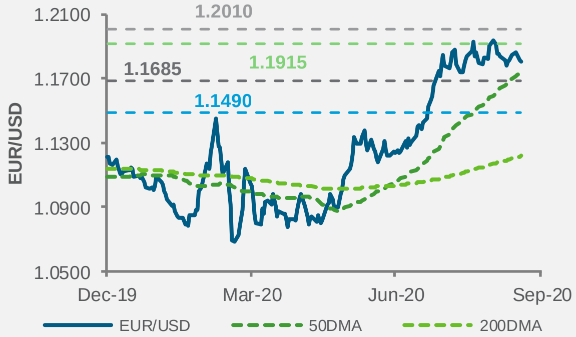
The outcome of the final pre-election Fed meeting brought few surprises. The USD gained tentatively against most currencies, except the range-bound JPY.

We expect more short-term USD gains ahead of the US election. Despite improving economic data, we are cautious about the likelihood of a risk asset pullback. Political uncertainty and other potential negative-sentiment triggers, combined with short-USD speculative positioning, create a scenario that should support the USD in the coming weeks. However, within the context of our 12-month bearish USD view, a short-term USD rally could provide attractive entry levels for our preferred currencies ahead of the next leg of the anticipated cyclical USD downtrend.

Robust EUR/USD technical support is around 1.1685 followed by 1.1490, which we expect to hold any corrective decline. AUD/USD has strong support around 0.7060, but a break of this level would likely lead to a decline to 0.6775. GBP/USD also faces Brexit uncertainty and could be more volatile in the coming weeks. GBP/USD support around 1.2700 should hold unless Brexit negotiations break down, in which case the risk shifts towards a move to 1.2200-1.2400 levels. The decline in USD/CNH is also approaching a key support area around 6.6700-6.7200, and we expect a correction higher towards 6.8500-6.9200 once the current decline falters.

We expect more short-term USD gains ahead of the US elections; however, we expect EUR/USD to hold above 1.1490 support in the event of a corrective decline

EUR/USD



Source: Bloomberg, Standard Chartered

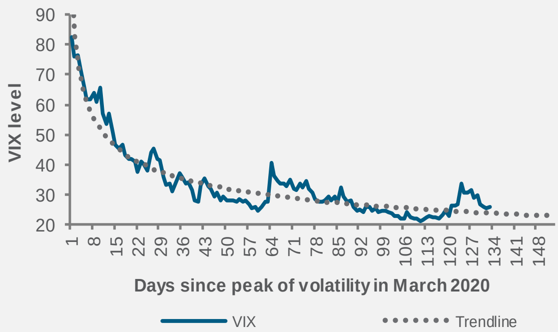
Will US equity market volatility decline further?

VIX, the measure of S&P500 index's implied volatility, spiked above 30 last week as we experienced the largest one-day sell-off in the index since June 2020. Since then, attempts to regain ground, especially in the technology sector, had invariably been met with selling pressure with volume. However, the speed of the pullback has slowed, resulting in a gradual pullback in volatility.

Our power model, which projects the path of volatility since its peak in the middle of March 2020, suggests volatility is still at an elevated level. As such, we believe there is value for yield-seeking investors to sell volatility to generate a yield in US equities, especially when the S&P500 index is only a few percentage points above key technical support around 3,300.

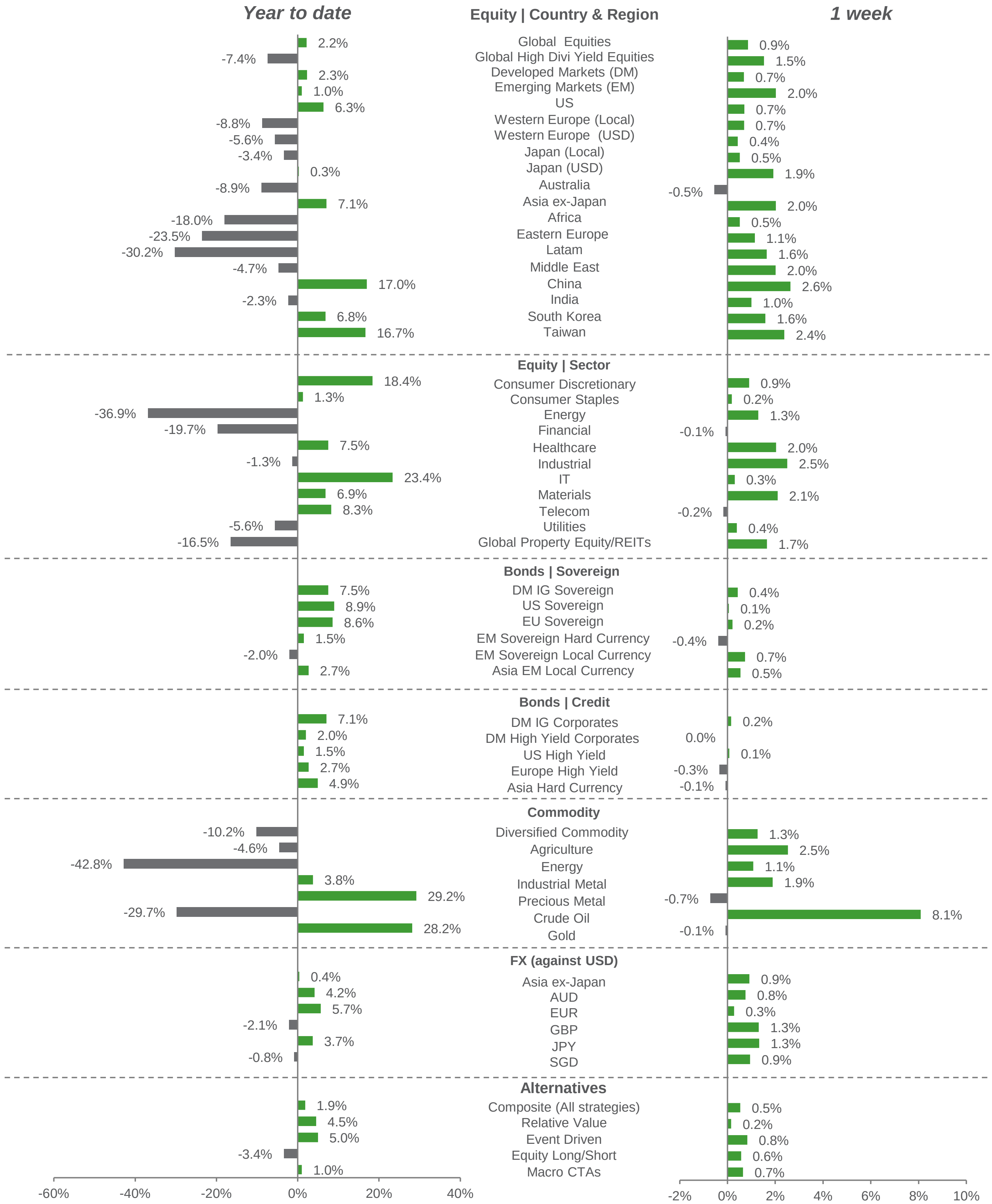
Our power model, which projects volatility's path since its peak in March, suggests volatility is still elevated; this offers investors opportunity to sell yield to generate yield

S&P500 implied volatility index (VIX) since March peak vs path/trendline predicted by our power model



Source: Bloomberg, Standard Chartered

Market performance summary*



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

*Performance in USD terms unless otherwise stated, 2019 performance from 31 December 2019 to 17 September 2020, 1 week period: 10 September 2020 to 17 September 2020

Our asset class views at a glance

Equities	▲
Asia ex-Japan	▲
US	▲
Euro area	▲
Japan	◆
Other EM	◆
UK	▼

Bonds (Rates)	▼
Govt EM local	◆
Govt DM IG	▼

Bonds (Credit)	▲
Asia USD	▲
Govt EM USD	▲
Corp DM HY	▲
Corp DM IG	▼

Alternative Strategies	◆
Equity hedge	◆
Event-driven	◆
Relative value	◆
Global macro	◆

Cash	▼
USD	▼
EUR	▲
GBP	▲
AUD	▲
CNY	◆
JPY	◆

Gold	▲

Source: Standard Chartered Global Investment Committee

Legend: ▲ Most preferred | ▼ Less preferred | ◆ Core holding

Economic and market calendar

	Event	This Week	Period	Actual	Event	Next Week	Period	Prior
MON								
TUE	CH	Industrial Production y/y	Aug	5.6%	EC	Consumer Confidence	Sep A	-14.7
	CH	Retail Sales y/y	Aug	0.5%				
	CH	Fixed Assets Ex Rural YTD y/y	Aug	-0.3%				
	EC	ZEW Survey Expectations	Sep	77.4				
WED	JN	Exports y/y	Aug	-14.8%	JN	Jibun Bank Japan PMI Composite	Sep P	45.2
	US	Retail Sales Ex Auto and Gas	Aug	0.7%	GE	GfK Consumer Confidence	Oct	-1.8
					FR	Markit France Composite PMI	Sep P	51.6
					EC	Markit Eurozone Composite PMI	Sep P	51.9
					UK	Markit/CIPS UK Composite PMI	Sep P	59.1
					US	Markit US Manufacturing PMI	Sep P	53.1
					US	Markit US Composite PMI	Sep P	54.6
THUR	US	FOMC Rate Decision (Lower Bound)	16-Sep	0.0%	JN	Nationwide Dept Sales y/y	Aug	-20.3%
	UK	Bank of England Bank Rate	17-Sep	0.1%	GE	IFO Current Assessment	Sep	87.9
	US	Building Permits	Aug	1470k	US	Powell, Mnuchin Testify Before Senate Banking Committee		
	US	Housing Starts	Aug	1416k	US	New Home Sales	Aug	901k
	US	Philadelphia Fed Business Outlook	Sep	15.0				
	JN	BOJ Policy Balance Rate	17-Sep	-0.1%				
FRI/SAT	JN	Natl CPI Ex Fresh Food, Energy y/y	Aug	-0.1%	EC	M3 Money Supply y/y	Aug	10.2%
	US	U. of Mich. Current Conditions	Sep P		US	Durable Goods Orders	Aug P	11.4%
					US	Cap Goods Orders Nondef Ex Air	Aug P	1.9%

Source: Bloomberg, Standard Chartered; key indicators highlighted in blue; *refers to Jan-Feb 2020 combined data
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

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