

Weekly Market View

Time to consolidate gains?

Investors are looking for fresh drivers to sustain the stellar rally in risk assets since March. Technical charts suggest fatigue. Strong data, more policy support and news about COVID-19 cures or vaccines could drive further upside. Resurgence of pandemic and US-China tensions are key risks

Equities: Risk of dividend yield cuts in Europe's energy sector underlines our cautious stance there. We prefer the technology sector in the US and China

Bonds: Asian High Yield bonds are likely to outperform US counterparts as Asian default rates likely to be lower

FX: EUR/USD and AUD/USD face near-term consolidation after strong rallies, with supports around 1.1000 and 0.6450, respectively

Time to consolidate gains

Also find out...

What are the implications of US-China technology sector engagement in 5G?

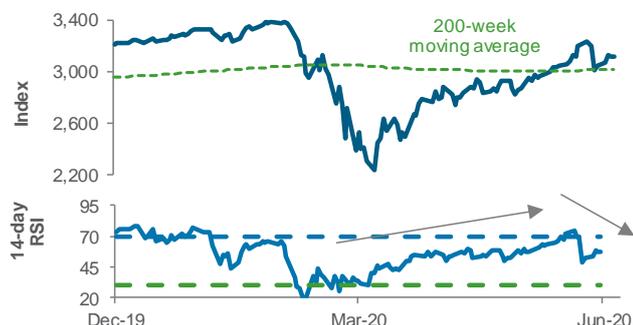
Are technical indicators pointing to a correction in risk assets?

Does the rally in High Yield and corporate bonds have room to extend further?

Chart of the week: Stocks are looking for the next driver to rally

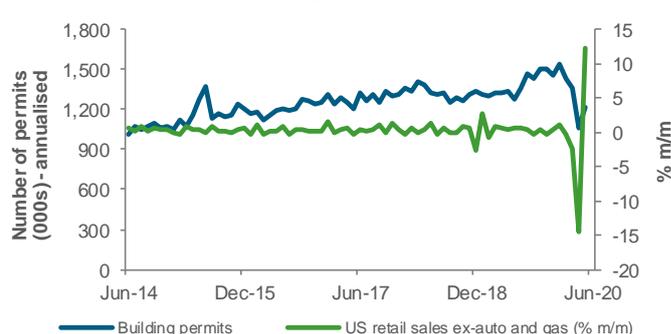
Technical charts indicate fatigue in the stock market rally, but a rebound in economic data from April's lows has provided strong support

US S&P500 index and Relative Strength Index (momentum indicator)



Source: Bloomberg, Standard Chartered

US retail sales and house building permits rebounded in May



Editorial

Time to consolidate gains?

The market is looking for fresh drivers to sustain the stellar recovery in risk assets since March lows. This week's rebound in global equities failed to make up for last week's pullback. The USD, a counter-cyclical indicator of risk sentiment, has recovered part of its losses from early June. Technical indicators are showing signs of fatigue (see page 5).

What could drive the next stage of the rally? The promising results of an inexpensive steroid drug for critically ill COVID-19 patients briefly galvanised the bulls. The market's reaction shows the focus remains on the dozens of organisations racing to find a cure or vaccine. Any breakthrough here would be significantly positive for risk assets as the established view is that a cure or vaccine is at least a year away.

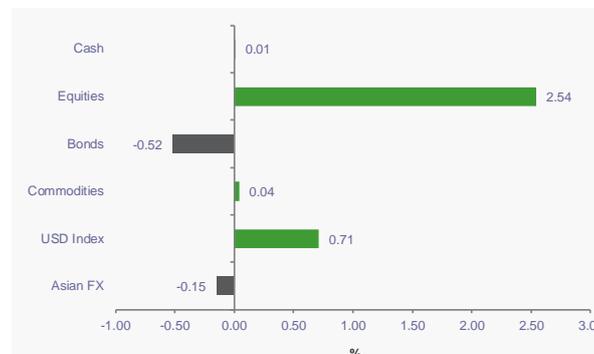
Meanwhile, economic data needs to do the heavy lifting to sustain the rally, and it did not disappoint this week. The rebound in US retail sales and housing data in May shows the economy is recovering from April's lows. Europe's surveys showed rising optimism about a recovery, while China's infrastructure spending surge shows credit stimulus is working.

As lockdowns are lifted, our view is that the unprecedented stimulus – which governments keep expanding (see page 3) – will turbo-charge the recovery. We see US and Euro area quarterly growth turning positive in Q3 20 (China likely turned positive in Q2). As growth recovers, corporate earnings and risk assets are likely to benefit. This view is supported by a rebound in 12-month forward earnings expectations. Surveys show investors are holding higher-than-average cash, which could fuel a rally.

The constructive outlook has its share of risks. The continued rise in new COVID-19 infections in Florida and Texas has led US authorities to warn of renewed lockdowns. Brazil and India remain hotspots. Meanwhile, deflationary pressures are building, especially in Europe. This raises pressure on all 27 EU members to approve a EUR 750bn spending plan and share the region's debt for the first time. A breakthrough would be a positive surprise for risk assets. Also, US-China tensions are simmering (see pages 3-4) and any escalation could trigger a market correction.

However, given our medium-term constructive view, we believe any such correction would be an opportunity to add to our preferred assets, including US and Asia ex-Japan equities, Emerging Market (EM) and Asia bonds and the EUR and AUD (see pages 4-6).

Global equities rebounded from the previous week's losses amid strong economic data; the USD's bounce partly highlights risks around a resurgence in COVID-19
 Benchmark market performance w/w*



Source: MSCI, JP Morgan, DJ-UBS, Citigroup, Bloomberg, Standard Chartered

*Week of 11 June 2020 to 18 June 2020

The S&P500 index has support 1.7% below current level

Technical indicators for key markets as on 18 June 2020

Index	Spot	1st support	1st resistance
S&P	3,115	3,063	3,146
STOXX 50	3,250	3,168	3,299
FTSE 100	6,224	6,108	6,297
Nikkei 225	22,491	21,821	22,872
Shanghai Comp	2,939	2,906	2,956
Hang Seng	24,465	24,001	24,705
MSCI Asia ex-Japan	646	632	653
MSCI EM	995	976	1,005
Brent (ICE)	41.6	39.7	42.6
Gold	1,724	1,721	1,729
UST 10Y Yield	0.70	0.68	0.74

Source: Bloomberg, Standard Chartered

The weekly macro balance-sheet

	Positive for risk assets	Negative for risk assets
COVID-19	<ul style="list-style-type: none"> UK scientists said an inexpensive steroid drug, dexamethasone, showed promising results for treating critically ill COVID-19 patients (though not for mild conditions). WHO welcomed the initial trials 	<ul style="list-style-type: none"> US authorities warned of renewed lockdowns as new cases surged in Texas, Florida Beijing imposed localised lockdowns amid new cases Cases in Brazil, India and South Africa continued to rise

Our view: The equity gains this week following promising results from a steroid drug trial for COVID-19 is yet another indication of how investors are focussed on a cure or a vaccine. Positive results from existing drugs/vaccines would speed up the time to implement treatments, which would significantly alleviate a key uncertainty confronting risk assets

Macro data and events		
<ul style="list-style-type: none"> US retail sales jumped a record 18% m/m in May, and Michigan Consumer Sentiment index rebounded from April's lows as lockdowns gradually lifted US building permits jumped 14% m/m and housing starts rose 4.3% m/m in May as low interest rates lifted demand The ZEW Survey showed increased expectations of a Euro area economic recovery China's infrastructure spending jumped 12% y/y in May, the fastest pace in two years, reflecting the government's renewed focus on reviving jobs and the economy China's industrial production rose 4.4% y/y and retail sales increased 0.8% m/m in May 	<ul style="list-style-type: none"> Euro area consumer inflation slumped further to 0.1% y/y in May, while UK inflation fell to a four-year low of 0.5% y/y, highlighting building deflationary pressures US continuing jobless claims stayed above 20 million, although initial jobless claims have declined for a record 11th week in a row Japan's exports slumped 28% y/y in May, highlighting the still-depressed state of global trade India-China border military skirmishes led to casualties Former US National Security Advisor Bolton's upcoming book about his experience in the Trump administration is likely to raise US political uncertainty 	

Policy developments		
<ul style="list-style-type: none"> The Fed unveiled plans to buy a broader range of corporate bonds from secondary markets Fed Chair Powell asked Congress for continued fiscal stimulus support President Trump proposed USD 1trn in infrastructure spending Germany unveiled a new EUR 130bn fiscal stimulus package BoE boosted its bond-buying programme by GBP 100bn Japan's approved a JPY 32trn package for businesses and households; BoJ boosted loan support to firms by JPY 110trn US allowed technology companies to work with China's Huawei on 5G standards 	<ul style="list-style-type: none"> The Fed, in its semi-annual report to Congress, warned of major vulnerabilities in the financial sector as the economic outlook remained "uncertain" and "alarming" 	

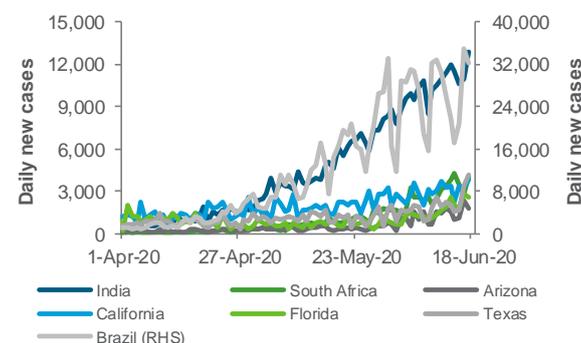
Our weekly net assessment: On balance, we see this week's COVID-19, macro data and policy developments as supportive of risk assets in the medium term (12m)

(+) factor: Improving US retail sales and housing, China infrastructure data; sustained policy support

(-) factor: Resurgence in COVID-19, disinflation, US political risk

New COVID-19 infections continue to rise across large southern US states and in major Emerging Markets such as Brazil, India and South Africa

New daily COVID-19 cases



Source: Bloomberg; Standard Chartered

Deflationary pressures are building, especially in Europe, which will likely lead authorities to further ease fiscal and monetary policies

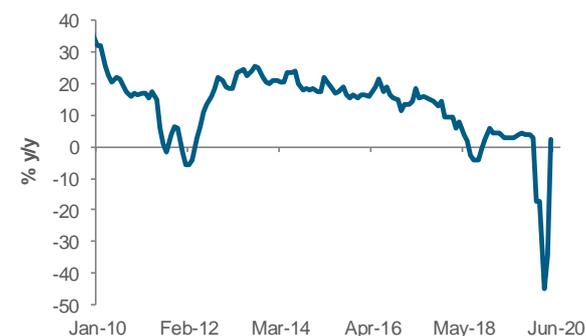
Euro area and UK consumer inflation



Source: Bloomberg, Standard Chartered

China's infrastructure investment rebounded sharply in May, indicating that targeted credit stimulus towards local governments is starting to have an impact

China's infrastructure investment growth, three-month moving average



Source: Bloomberg; Standard Chartered

Top client questions

Q Is there a risk of dividend cuts in Europe's energy sector?

After an initial rally in March, the European energy sector has been stuck in a tight range since mid-April with investors and companies digesting the longer-term implications of the coronavirus on demand for oil and Europe's possible accelerated transition to a low carbon future. Select companies have already cut dividends, and there are rising expectations that other large companies will follow suit.

The European energy sector is valued on a 12-month forward price-earnings ratio of 32x, versus a long-term average of 12x, following a substantial drop in earnings expectations for this year. The 12-month forward dividend yield is currently at 7.0%, significantly above the long-term average of 5.5%, but this is likely to fall on further dividend cuts by companies.

Long-term oil price assumptions have started to decline, with some European oil majors cutting assumptions to between USD 50-60/bbl. The reduction in the long-term oil price assumption represents a significant change and has resulted in individual companies reducing the value of assets held on their balance sheets by USD 10-20bn. The reduction also calls into question the viability of select oil projects.

Taken together, we see the reduction in long-term energy prices and increased provisions for assets held on balance sheets as prudent, but likely to undermine the dividend outlook. We view European energy as a least preferred sector, reflecting in part concerns over the long-term outlook for demand and dividend sustainability.

Q What are the implications of US telecom companies engaging with Huawei on 5G standards?

The US government recently announced that telecom companies will be allowed to work with Huawei on the development of 5G mobile communication standards. Restrictions on export of semiconductors to Huawei and its affiliates remain in place.

The updated policy addresses risks of the US being left behind in the development of standards and patents for 5G networks if it cannot collaborate with Huawei on global industry standards. While China might have preferred to develop its own standards, that would have come with the risk that its standards would not be adopted by global telecom networks, thus reducing demand for its services.

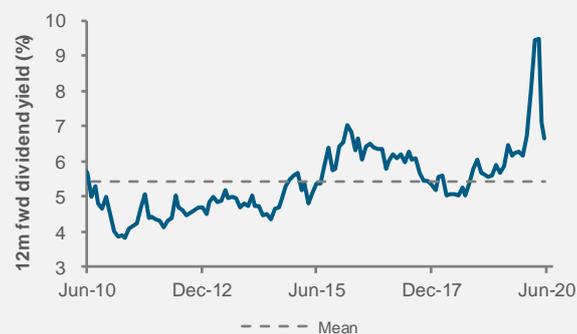
Separately, China is working hard to be less technologically reliant on the US. China's state-sponsored semiconductor champion recently announced plans to dual list on the Shanghai Stock Exchange to raise capital to build a chip plant capable of producing 12-nanometre chips for domestic integrated circuit design companies. This technology standard remains behind the industry leader, which recently announced plans to build a 5-nanometre chip plant, and the technology to produce semiconductors is challenging to master.

Reports have estimated that China may take four years to match the US's current leadership in chip technology. However, China is catching up and has the advantage of a large domestic market.

Overall, we view the US policy towards China on technology as merely slowing the inevitable, as opposed to altering the direction of the sector, which we view as preferred in both China and the US.

European energy companies are likely to cut dividends over the next 12 months

12-month forward dividend yield for European energy sector



Source: FactSet; Standard Chartered

Crude oil prices have rebounded from March lows, but the long-term outlook for prices remains uncertain

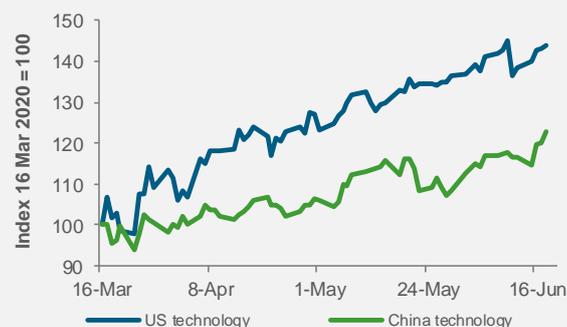
US WTI crude oil price



Source: Bloomberg; Standard Chartered

We prefer technology sector equities in both the US and China

Relative performance of MSCI US technology and MSCI China technology sectors (Indexed: 100 = 16 March)



Source: Bloomberg; Standard Chartered

Top client questions (cont'd)

Q Are technical indicators pointing to a correction in risk assets?

Our market diversity indicator is not pointing to an imminent reversal in the S&P 500 index. The indicator over a 55-day window signalled a red flag earlier this month, consistent with the recent equity pullback. However, it is currently at 1.39, above the 1.25 level which usually indicates heightened risk of a near-term reversal.

On technical charts, the gap lower last week, coupled with stalling momentum (14-day Relative Strength Index), indicates that the three-month long rally is showing signs of fatigue. To be fair, these could be viewed as a necessary, but not sufficient, condition for a reversal. We believe a break below support at 2,767 (11% below Thursday's close), after an initial support break at 3,063, is likely needed to pose a risk to the three-month long uptrend.

We extended our analysis of market diversity to the S&P 500 information technology sector, the primary driver of S&P 500 returns. Despite not bearing the same brunt as the S&P 500 index in the recent correction, our 55-day market diversity indicator for US information technology remains comfortably above the red line. On technical charts, a break below the 27 May low of 1,657 (8.4% below Thursday's close) would likely be needed to indicate that the upward pressure from March had eased.

In sum, while risk assets are looking overbought, quantitative and technical indicators suggest it is too soon to conclude the recent pause is the start of a broader correction.

Q Do you think the current rally in HY and other corporate bonds has more room to extend?

US High Yield (HY) bonds and Emerging Market (EM) sovereign and corporate bonds have witnessed a spectacular rally over the past two months, helped by the improving risk sentiment and higher oil prices. Given the strong performance, we believe the room for continued outperformance has reduced and that a more nuanced views will be needed from here.

US HY bond yield premiums over Treasuries have declined by more than 500bps since March. This means current valuations are no longer unusually (more than 1 standard deviation) cheap relative to history. The scope for further outperformance from here likely depends on the default outlook. At current levels, markets are likely pricing in a 7-8% default rate. We still see room for more spread compression if default rates get capped around these levels and decline thereafter. However, the possibility of higher-than-expected defaults is a risk, holding us back from a much more constructive view on the asset class.

We are modestly more constructive on Asian HY bonds. Property sales in China have rebounded strongly and economic activity has picked up. The relatively large exposure to the Chinese property sector, and to less vulnerable sectors more generally, leads us to believe that default rates are likely to be lower than in US HY. This suggests Asian HY USD bonds have room to outperform their US HY peers.

US equity technical indicators are pointing to fatigue in the rally, although it is too soon to conclude that the recent pause is the start of a broader correction

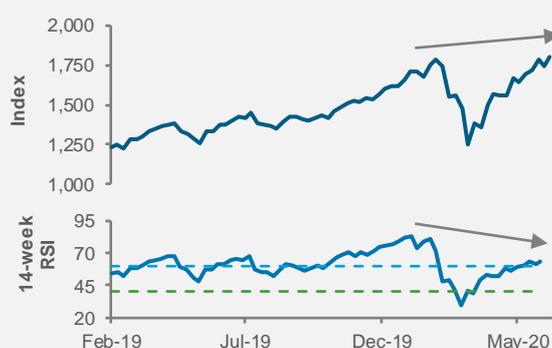
US S&P500 index and 14-day Relative Strength Index (momentum indicator)



Source: Bloomberg; Standard Chartered

The US S&P500 technology sector index needs to break below 1657 to indicate that the upward pressure from March has eased

S&P500 technology sector index and 14-week Relative Strength Index (momentum indicator)



Source: Bloomberg; Standard Chartered

The difference in yield premiums between Asian and US High Yield (HY) bonds is likely to decline, in our view, as default rates in Asia are likely to be lower

Difference in yield premiums between Asian and US HY bonds



Source: Bloomberg; Standard Chartered

Top client questions (cont'd)

Q Are the rallies in the EUR and the AUD over?

A near-term outlook for consolidation in risk assets means we believe the USD is likely to further recover recent losses, albeit while maintaining its longer term downtrend.

EUR/USD is consolidating after a rally from 1.0725 to 1.1420. We expect initial support to be within 1.1120-1.1150 as the outlook for a more robust European recovery shows promise.

We believe Germany's commitment to fiscal stimulus, which will largely be deployed in H2 20, to be a key factor in limiting any near-term EUR weakness. Should this technical support break, we would look for a base around 1.1000 as the pair looks to reassert its bullish trend towards 1.1420 and 1.1495.

AUD/USD has a larger rally to consolidate, having stretched from 0.5500 to above 0.7050 in less than three months from mid-March. Technicals suggest that the AUD has set the stage for further medium-term strength, but we are more cautious about the near term.

The domestic economy continues to be weak, and employment may take time to improve, especially if border controls remain in place and uncertainty around exports to China continues. Initial resistance is expected to be within 0.7000-0.7060, with further technical hurdles at 0.7130 and 0.7200. We believe AUD/USD may drift lower towards support at 0.6670. A break below support would suggest a deeper setback towards 0.6450-0.6500 before the next leg of the rally begins.

EUR/USD has strong support at 1.1000 as it consolidates gains over the past month; we believe the medium-term uptrend remains intact

EUR/USD



Source: Bloomberg; Standard Chartered

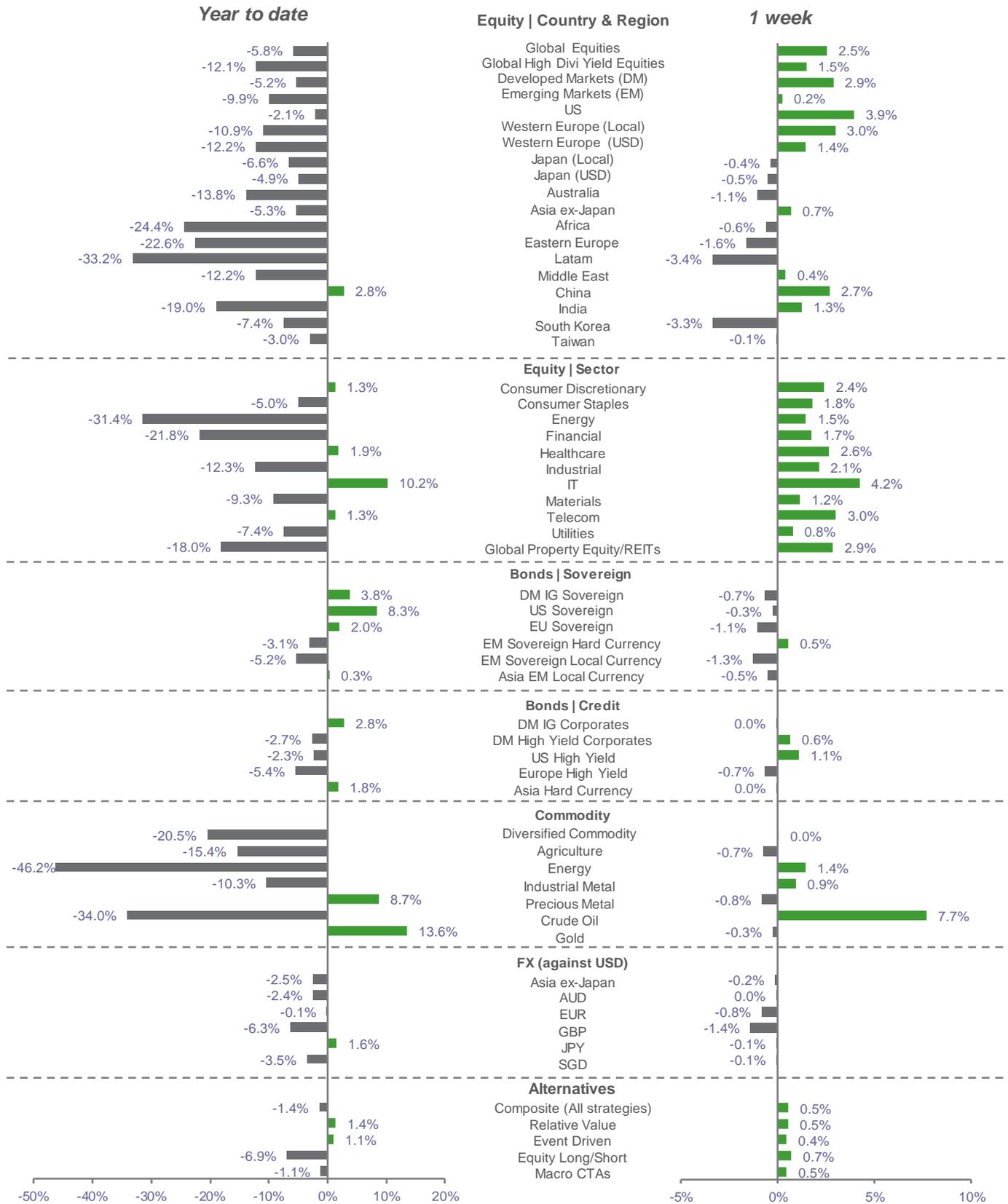
We are more cautious about AUD/USD in the near-term after the sharp rebound since March, although we remain constructive on the pair in the medium-term

AUD/USD



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 18 June 2020, 1 week period: 11 June 2020 to 18 June 2020

Economic and market calendar

	Event	Next Week	Date	Period	Expected	Prior
MON	EC	Consumer Confidence	22-Jun-2020	Jun A	–	-18.8
	JN	Jibun Bank Japan PMI Composite	23-Jun-2020	Jun P	–	27.8
TUE	JN	Nationwide Dept Sales y/y	23-Jun-2020	May	–	-72.8%
	FR	Markit France Composite PMI	23-Jun-2020	Jun P	–	32.1
	GE	Markit/BME Germany Composite PMI	23-Jun-2020	Jun P	–	32.3
	EC	Markit Eurozone Composite PMI	23-Jun-2020	Jun P	–	31.9
	UK	Markit/CIPS UK Composite PMI	23-Jun-2020	Jun P	–	30
	US	Markit US Composite PMI	23-Jun-2020	Jun P	–	37
	US	New Home Sales	23-Jun-2020	May	630k	623k
	WED	JN	PPI Services y/y	24-Jun-2020	May	–
GE		IFO Expectations	24-Jun-2020	Jun	–	80.1
THUR	US	Cap Goods Orders Nondef Ex Air	25-Jun-2020	May P	–	-6.1%
FRI/ SAT	EC	M3 Money Supply y/y	26-Jun-2020	May	–	8.3%
	US	Personal Income	26-Jun-2020	May	-5.0%	10.5%

	Event	This Week	Date	Period	Actual	Prior
MON	CH	Industrial Production y/y	15-Jun-2020	May	4.4%	3.9%
	CH	Retail Sales y/y	15-Jun-2020	May	-2.8%	-7.5%
	CH	Fixed Assets Ex Rural YTD y/y	15-Jun-2020	May	-6.3%	-10.3%
	IN	Exports y/y	15-Jun-2020	May	-36.5%	-60.3%
TUE	EC	ZEW Survey Expectations	16-Jun-2020	Jun	63.4	51.0
	US	Retail Sales Ex Auto and Gas	16-Jun-2020	May	12.4%	-14.4%
	US	Industrial Production m/m	16-Jun-2020	May	1.4%	-12.5%
	US	Capacity Utilization	16-Jun-2020	May	64.8%	64.0%
	JN	BOJ Policy Balance Rate	16-Jun-2020	16-Jun	-0.1%	-0.1%
WED	JN	Exports y/y	17-Jun-2020	May	-28.3%	-21.9%
	US	Building Permits	17-Jun-2020	May	1220k	1066k
	US	Housing Starts	17-Jun-2020	May	974k	934k
THUR	UK	Bank of England Bank Rate	18-Jun-2020	18-Jun	0.1%	0.1%
	US	Philadelphia Fed Business Outlook	18-Jun-2020	Jun	27.5	-43.1
	IN	BoP Current Account Balance	18-Jun-2020	1Q	–	-\$1.40b
FRI/ SAT	UK	Retail Sales Ex Auto Fuel y/y	19-Jun-2020	May	–	-18.4%
	GE	PPI y/y	19-Jun-2020	May	–	-1.9%
	EC	European Council meeting to discuss EUR 750bn pandemic recovery fund	19-Jun-2020			

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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