

Weekly Market View

Watching economies re-open

We expect a near-term setback to the risk-asset rally amid renewed geopolitical risks and a very gradual re-opening of economies

Equities: We believe averaging-in would be a good way to mitigate short-term uncertainty

Bonds: Markets are likely underestimating default risks in High Yield bonds. We prefer Asian and Emerging Market USD bonds

FX: We see bouts of near-term volatility in AUD, NZD as opportunities to add medium-term exposure

Watching economies reopen

Also find out...

Should we sell in May and go away?

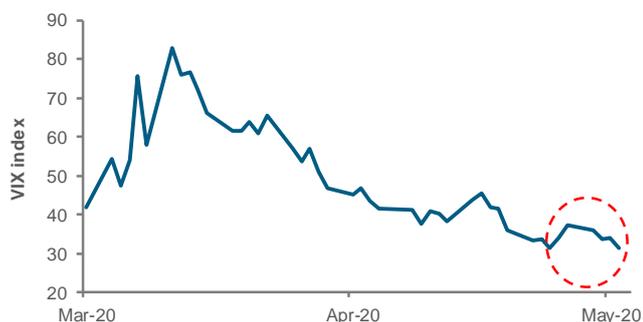
What are the implications of the Q1 earnings season?

What is our view on Developed Market High Yield bonds?

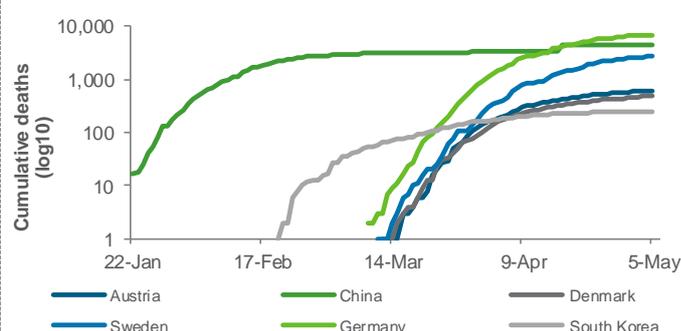
Chart of the week: As economies open, Trump revives political risk

Equity volatility briefly rebounded after Trump's rhetoric against China; focus likely to turn to COVID-19 trends as economies reopen

S&P500 Volatility index (VIX)



Cumulative COVID-19 fatality numbers in reopened economies



Source: Johns Hopkins University, Bloomberg, Standard Chartered

Editorial

Watching economies re-open

May had a rocky start with US President Trump reviving geopolitical uncertainty, but risk assets recovered subsequently as the focus turned to more economies re-opening after weeks of lockdowns. In the coming weeks, markets will assess how the early starters – Austria, Denmark and Germany in Europe, China and South Korea in Asia and Texas and some other states in the US – succeed in balancing the desire to resume normal economic activity as quickly as possible, while trying to avoid a second wave of COVID-19 infections. The outlook is more challenging in Emerging Markets (EMs) such as India and Brazil as testing rates rise.

COVID-19 vaccines and treatments are other potential sources of surprise for markets in the coming weeks. The US approval for the drug Remdesivir shows how governments are willing to hasten the approval process to try out new treatments. Israel's claim of a breakthrough in developing an antibody to treat the virus is another notable development.

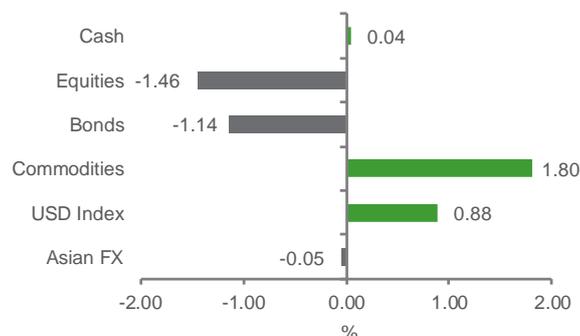
The sharp rebound in oil prices this week, as OPEC production cuts kick in, partially explains the tightening of yield premiums in US High Yield (HY) bonds, though we would caution against adding exposure here until we see signs of a global oil demand recovery. EM bonds have benefitted from the return of foreign inflows in April, a trend we are closely following.

Against some of these positive signs, President Trump's rhetoric against China revives risks. We do not expect this to overwhelm other positive trends, ie, expected growth and corporate earnings recovery in the next 6-12 months on the back of unprecedented stimulus (see page 4 for earnings outlook). Heightened geopolitical uncertainty could jeopardise any recovery and Trump's chance of winning the November presidential election. Reports of high-level US-China trade talks next week suggest both sides recognise the risks of further escalation in tensions.

On balance, we expect near-term weakness on the back of renewed geopolitical risks and upcoming weak data. This is reflected in money markets now pricing in negative US interest rates. Any signs of a second wave of the pandemic could further heighten volatility. However, we believe such short-term pullbacks should provide opportunity to average into our preferred assets - US and Asia ex-Japan equities and Asian and EM USD bonds. Gold remains a hedge against the ensuing volatility.

Global equities pulled back and USD rose early in May on renewed geopolitical risk; Europe dragged global bonds lower; oil rebounded sharply amid OPEC output cuts

Benchmark market performance w/w*



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

*Week of 30 April 2020 to 07 May 2020

US equity market technicals have turned neutral from positive; Asian equity technicals remain positive

Technical indicators for key markets as on 07 May 2020

Index	Spot	1st support	1st resistance	Short-term trend
S&P	2,881	2,792	2,955	→
STOXX 50	2,881	2,705	2,947	↗
FTSE 100	5,936	5,597	6,030	↗
Nikkei 225	19,675	18,850	20,350	↗
Shanghai Comp	2,872	2,760	2,940	↗
Hang Seng	23,981	23,500	24,500	↑
MSCI Asia ex-Japan	595	577	610	↗
MSCI EM	899	864	930	↗
Brent (ICE)	29	23	36	↗
Gold	1,712	1,655	1,745	↑
UST 10Y Yield	0.64	0.30	0.92	↓

Source: Trading Central, Standard Chartered

Note: Arrows represent short-term trend opinions

Factors to watch

Some forward-looking economic indicators picking up

Business confidence indicators for April predictably reflected the shock to economies from the COVID-19-related lockdowns. The indicators for US manufacturing and non-manufacturing (ISM) slumped to the weakest levels since 2009. In the Euro area, business confidence plunged to the lowest on record. Deflationary pressures are also building, especially in the Euro area, with the plunge in oil prices.

However, there are signs of a revival in medium-term growth expectations. As Euro area economies re-open, the Sentix Investor Confidence indicator (see chart) shows the positive divergence between forward expectations and current conditions. This partly explains the rebound in risk assets in the past month – equity markets discount the future, and the indicator suggests the 6-12-month outlook is improving.

Trump revives geopolitical uncertainty

We previously highlighted the risk of a renewed trade tensions should President Trump lose popularity before November's election. Since WWII, no US incumbent has secured a second term while facing a recession during an election year. The COVID-19 pandemic has further complicated matters. The President is responding by trying to shift the blame to China. We believe the threats are mostly political "posturing" since sustained trade tensions would hurt the economy and Trump's re-election prospects. Tariffs are double-edged swords and replacing global supply chains out of China would take years. Nevertheless, we expect volatility to occasionally pick up leading into the election.

German court ruling raises medium-term Euro area risks

The ruling by the German Constitutional Court on the legality of the ECB's bond-purchase programme raises some medium-term uncertainty about the ECB's ability to "do whatever it takes" to stabilise the Euro area's financial markets, in our view. While the ECB should be able to satisfy the court that its 2015 bond-buying programme was in line with its monetary policy objectives, it may struggle to justify the latest Pandemic Emergency Purchase Programme (PEPP). The latest plan relaxed prior limits on the extent of bonds it can buy from each country and the requirement to buy only Investment Grade bonds, benefitting weaker Euro area members such as Italy and Greece. While ECB President Lagarde renewed her pledge to "take all possible measures" to counter the crisis, questions about the legality of the PEPP increases the urgency of Euro area members to overcome resistance from some members and jointly finance a spending package through common bond sales. Any delays could increase the risk for Euro area markets.

Can oil's recovery last?

WTI crude oil prices have rebounded sharply since hitting a record low on 21 April as OPEC's planned production cuts kick in. Prices were also boosted by lower-than-expected US inventory builds (especially in Cushing) on hopes that a protracted rebalancing of excess supply is already underway. However, we would caution against a sustained rally in prices given the storage constraints, which suggest there is an elevated risk of a repeat of price volatility seen in end-April when prices of the May contract briefly turned negative. Also, global floating storage remains at elevated levels. Hence, we believe further gains for WTI crude oil prices will be harder to come by unless we see a sustained rebound in global demand for crude, which in turn depends on the pace of the revival in global economic activity.

Euro area forward-looking economic indicators are picking up, though current conditions remain dire

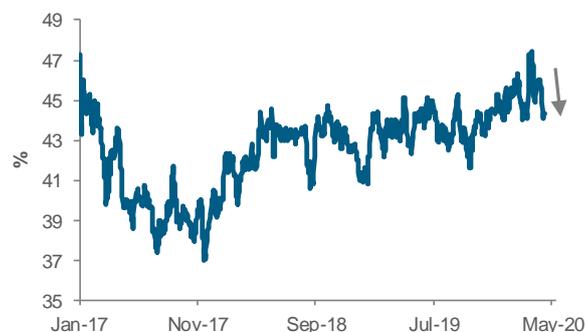
Euro area's Sentix Investor Confidence indices for current conditions and for six-month forward expectations



Source: Bloomberg; Standard Chartered

Geopolitical risk likely to rise if President Trump's approval ratings continue to decline

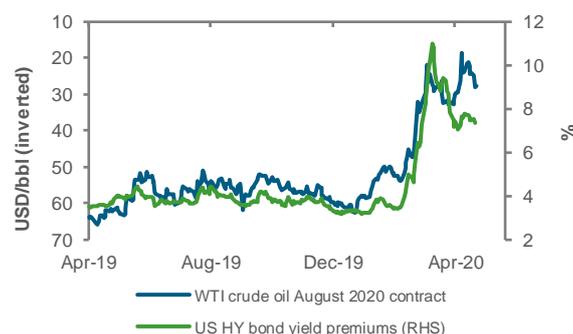
President Trump's approval rating



Source: RealClearPolitics; Bloomberg; Standard Chartered

WTI oil price recovery unlikely to be sustained until global demand picks up; increase in equity market volatility is likely to undermine US HY bonds again

WTI crude oil (contract for August, inverted) and US HY bond yield premium over Treasuries



Source: Bloomberg, Standard Chartered

Top client questions

Should we sell in May and go away?

The chart on the right shows that six-month returns from November-April have on average been higher than those from May-October, even if this seems less pronounced in the last five years. Our recent *Global Market Outlook* publication also cautioned investors on the near-term risks to equities. We highlighted the following risk factors: potential disappointment with the pace of economies' reopening, elevated valuations, technical charts have turned neutral from positive and the oil price collapse. We can add geopolitical risk to the list now, as US-China relations potentially deteriorate again. And the US S&P500 is consolidating some of the sharp bounce seen in April off the March lows. Technically, there is a risk that key support levels could be broken near-term and S&P500 could weaken further towards 2,727.

However, note in the adjoining chart that the average six-month returns in May-October are still positive. So, investors who "sold" would have forgone this return. The average number also conceals differences in each period; in the last six months for instance, US equities had a negative 4% return and the volatility in these six months has been significant, with a 34% peak to trough. Thus, each period has its own drivers, and the "seasonal average" does not dictate asset price movements. Against the short-term risk factors, we see unprecedented stimulus, with authorities willing to do "whatever it takes" and a peaking of new COVID-19 cases globally. We continue to be positive on equities over 12 months and believe an averaging-in approach is a good way to address short-term uncertainty.

What are the implications of the Q1 earnings season?

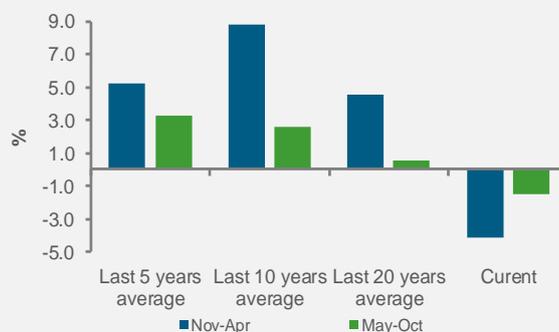
A total of 70% of companies in the S&P500 have reported so far, with earnings 3% better than expected on average. This is slightly worse than the average 5% beat seen in recent reporting seasons. Financial sector earnings surprised negatively as banks built up significant reserves for credit provisions, predominantly against credit card loans, as well as corporate loans across multiple sectors, notably in oil and gas. Consumer spending overall, and travel-related expenditure in particular, has dropped significantly, though consumer staples saw some "stocking up" purchases. On a slightly positive note, credit card companies that track global consumer spending have seen a stabilisation in April, albeit at very low levels. eCommerce volumes are accelerating significantly in the lockdown environment. The technology sector, which has turned positive YTD, contributed to a positive earnings surprise as cloud-related investments continue to grow; work-from-home boosted hardware and software expenditures.

Companies have been generally cautious with forward guidance or omitting them altogether given the unprecedented uncertainty facing the global economic outlook. As seen in the chart, 2020 earnings growth expectations have been gradually lowered as the earnings season progressed, but against that, 2021 earnings growth has been gradually raised as well. Increasingly, we see that the equity market is willing to look through the weakness in 2020 for a recovery in 2021.

We prefer Asia ex-Japan equities, with the region in a more mature COVID-19 infection cycle. US equities are also preferred, supported by low bond yields and the strong policy stimulus.

Equity market returns have generally been lower in May-Oct period than in Nov-Oct stretch, although this year we enter May after a pronounced drawdown

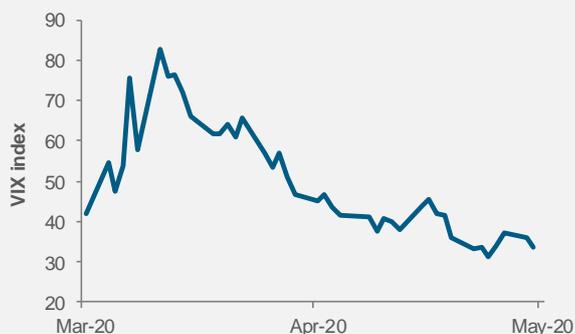
Average S&P500 index returns in Nov-Apr and May-Oct period over different periods



Source: FactSet; Standard Chartered

The pullback in equity market volatility underscores reduced risks since March following the unprecedented stimulus measures taken by authorities worldwide

S&P500 volatility index (VIX)



Source: Bloomberg; Standard Chartered

US earnings growth expectations for 2020 have been downgraded, while those for 2021 have been upgraded

Consensus S&P500 index earnings expectations for 2020 and 2021



Source: Refinitiv; Standard Chartered

Top client questions (cont'd)

Q What is your view on DM HY bonds, given the attractive yield on offer and a reduction in yield premiums over the past week?

Over the past week, Developed Market (DM) High Yield (HY) bond yield premiums have declined on the back of a sharp reduction in bond market volatility (US Treasury volatility is back to pre-COVID levels), Fed's plans to buy some HY debt which were recently rated as Investment Grade, and a rebound in oil price. Despite offering an attractive yield of over 9%, we view DM HY bonds as a core holding.

If we look at past recessions, default rates for HY bonds have typically peaked well after the trough in economic activity. The aggregate credit quality has also declined, as evident from the flurry of ratings downgrades for US and European HY bonds. There is a risk default rates could reach, if not exceed, Global Financial Crisis levels if the current economic downturn is longer than a few months.

Hence, while the yield on offer and short maturity profile of the HY bonds are certainly attractive, we believe they are balanced by a deterioration in credit fundamentals and rise in default risks, something the market may be underestimating.

Q What is the outlook for the AUD and the NZD?

Our 12-month view is bullish for AUD/USD, and we expect NZD/USD to follow suit. On a 1-3-month time horizon, the outlook is more mixed, and we anticipate both currency pairs trading in a range, with bouts of volatility providing an opportunity to accumulate the AUD and the NZD.

Both Australia and New Zealand have managed the COVID-19 outbreak quickly and are emerging from lockdowns having been strongly supported with monetary and fiscal stimulus. There are plans for a "trans-Tasman bubble", a first stage of cross-border travel relaxation, but both governments have stated that a wider international reconnection could take some time. This positive domestic sentiment should enable both countries to take advantage of a global growth rebound and the expected increased stimulus from China.

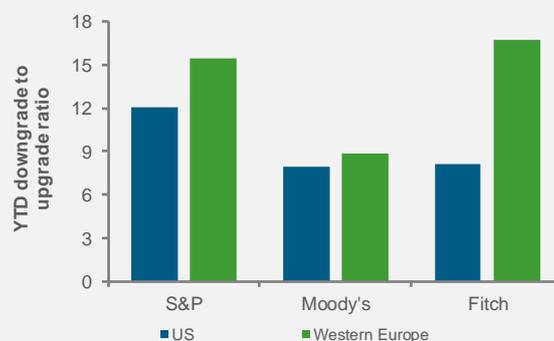
One potential "risk-off" driver is the rising US-China tensions, and what impact this might have on China's broader trade relations. Other risks that could cap the strength of the AUD and the NZD might be a sharper setback in US equities following the recent strong rise and fear of a second virus wave as global lockdowns are unwound.

From a technical perspective, AUD/USD has recovered almost 70% of the steep decline since March, and some consolidation is increasingly likely. Setbacks within the rally have been small thus far, but a more significant dip towards support at 0.6270 could provide an opportunity for investors to accumulate in the coming weeks. We see stronger support between 0.6035 and 0.6165 if the initial support breaks. If the broad risk sentiment continues to improve, we anticipate two strong levels of technical resistance at 0.6675 and around 0.6820.

NZD/USD has followed the same chart pattern as AUD/USD, but with less volatility. We expect initial support at 0.5900, with a stronger technical potential base between 0.5740 and 0.5820. Tough resistance lies above the current spot at 0.6265 and around 0.6500.

Rating agencies have significantly downgraded corporate debt issues this year as the COVID-19 crisis raises default risks

YTD downgrade-upgrade ratio at various rating agencies for the US and Europe



Source: Bloomberg, Standard Chartered

AUD/USD has recovered almost 70% of the steep decline in March and some consolidation is likely

AUD/USD



Source: Refinitiv; Standard Chartered

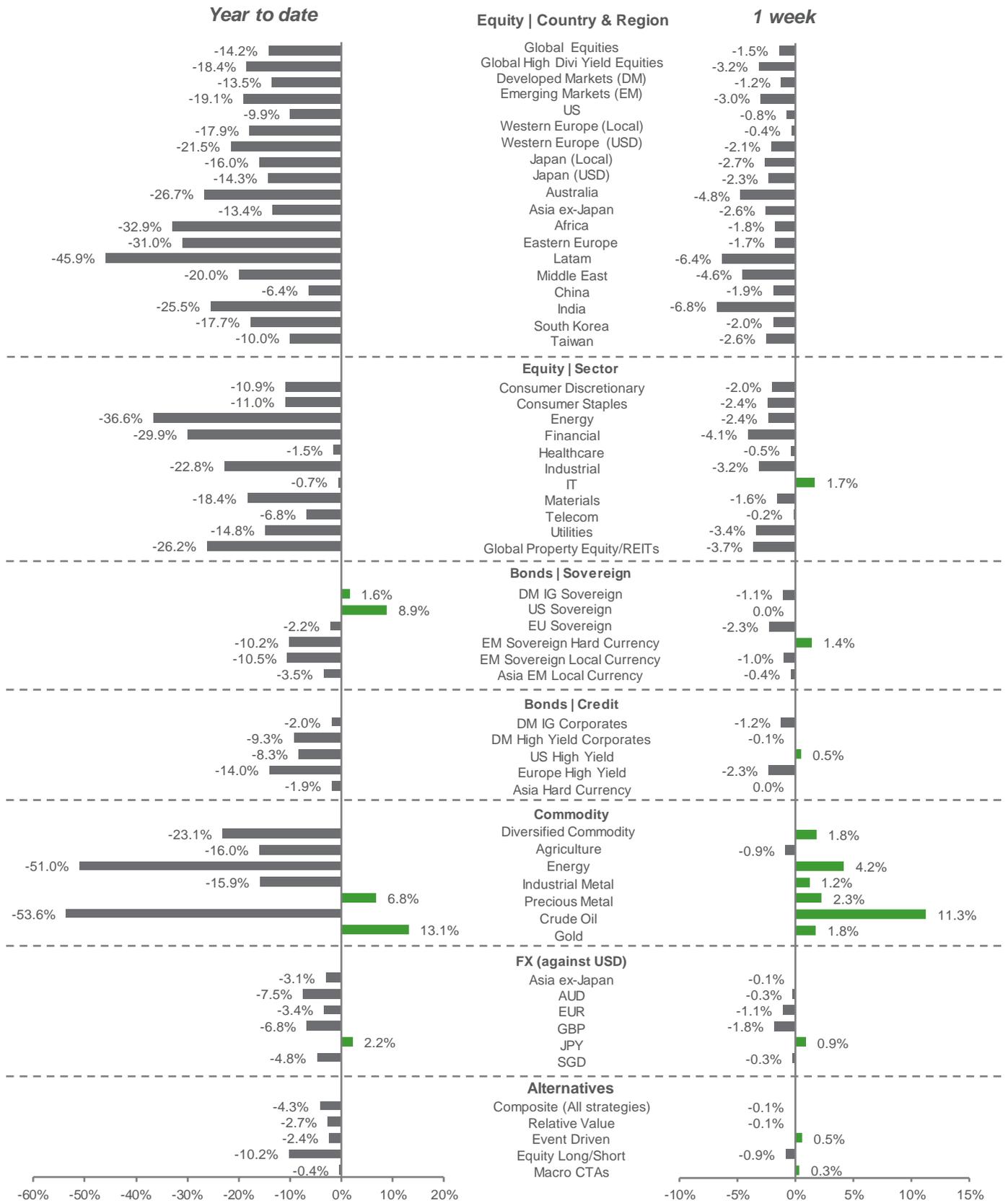
NZD/USD has followed the same pattern as AUD/USD, but with less volatility

NZD/USD



Source: Refinitiv; 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 07 May 2020, 1 week period: 30 April 2020 to 07 May 2020

Economic and market calendar

	Event	Next Week	Date	Period	Expected	Prior
MON						
TUE	CH	PPI y/y	12-May-2020	Apr	-2.6%	-1.5%
	CH	CPI y/y	12-May-2020	Apr	3.7%	4.3%
	IN	Industrial Production y/y	12-May-2020	Mar	-8.0%	4.5%
	US	CPI Ex Food and Energy y/y	12-May-2020	Apr	1.7%	2.1%
WED	JN	BoP Current Account Adjusted	13-May-2020	Mar	–	¥2378.1b
	UK	GDP y/y	13-May-2020	1Q P	–	1.1%
	US	PPI Ex Food and Energy y/y	13-May-2020	Apr	–	1.4%
THUR	JN	Machine Tool Orders y/y	14-May-2020	Apr P	–	-40.7%
FR/SAT	CH	Industrial Production y/y	15-May-2020	Apr	1.5%	-1.1%
	CH	Retail Sales y/y	15-May-2020	Apr	-5.2%	-15.8%
	CH	Fixed Assets Ex Rural YTD y/y	15-May-2020	Apr	-8.5%	-16.1%
	US	Retail Sales Ex Auto and Gas	15-May-2020	Apr	–	-2.8%
	US	Industrial Production m/m	15-May-2020	Apr	-10.8%	-5.4%
	US	Capacity Utilization	15-May-2020	Apr	63.3%	72.7%
	US	U. of Mich. Sentiment	15-May-2020	May P	69.0	71.8
	IN	Exports y/y	15-May-2020	Apr	–	-34.6%
	Event	This Week	Date	Period	Actual	Prior
MON	SK	Markit South Korea PMI Mfg	04-May-2020	Apr	41.6	44.2
	EC	Sentix Investor Confidence	04-May-2020	May	-41.8	-42.9
TUE	EC	PPI y/y	05-May-2020	Mar	-2.8%	-1.4%
	US	Trade Balance	05-May-2020	Mar	-\$44.4b	-\$39.8b
WED	IN	Markit India PMI Composite	06-May-2020	Apr	7.2	50.6
	GE	Factory Orders WDA y/y	06-May-2020	Mar	-16.0%	1.9%
	UK	Markit/CIPS UK Construction PMI	06-May-2020	Apr	8.2	39.3
	EC	Retail Sales y/y	06-May-2020	Mar	-9.2%	2.5%
THUR	CH	Caixin China PMI Composite	07-May-2020	Apr	47.6	46.7
	UK	Bank of England Bank Rate	07-May-2020	7-May	0.1%	0.1%
	GE	Industrial Production WDA y/y	07-May-2020	Mar	-11.6%	-1.8%
	CH	Exports y/y	07-May-2020	Apr	3.5%	-6.6%
FR/SAT	GE	Exports SA MoM	08-May-2020	Mar	–	1.2%
	US	Change in Nonfarm Payrolls	08-May-2020	Apr	–	-701k
	US	Unemployment Rate	08-May-2020	Apr	–	4.4%
	US	Average Hourly Earnings y/y	08-May-2020	Apr	–	3.1%

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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