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WM Chief Investment Office
26 July 2021

Weekly Market View

What to watch this summer

The August-October period tends to be seasonally lacklustre for equity markets, but this year we are focussing on three key issues. The UK experiment with the idea of living with COVID-19 after adequate vaccinations could show the world a path out of the pandemic.

Corporate Q2 earnings are another bellwether. Sustained positive surprises should help equity markets continue to climb the 'wall of worry'. Finally, we expect policymakers to stay accommodative, sustaining the global economic expansion.

Equities: The US equity market uptrend remains intact, based on technical charts and continued positive earnings beats.

Bonds: We believe valuations in Asia High Yield USD corporate bonds are looking increasingly attractive, despite stress in the China real estate sector.

FX: We expect the GBP to benefit from the UK's 'vaccinate and live with it' strategy.

+

What are the implications of China's policy easing on its equities and bonds?

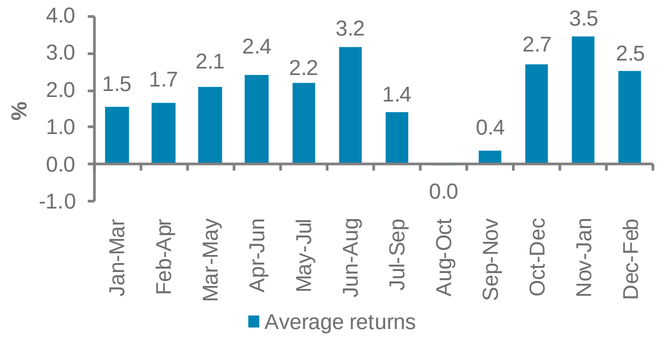
Are US equities at the start of a deeper correction?

What are technical charts saying about global and Asia stocks & crude oil?

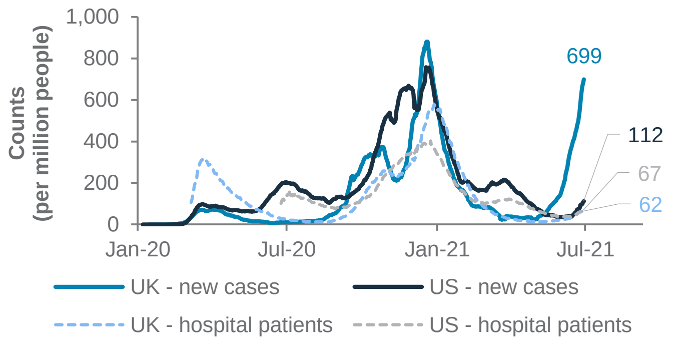
Charts of the week: The vaccination effect?

August-to-October period is seasonally lacklustre for markets. Potential 3rd COVID-19 wave adds uncertainty

3m average rolling returns of S&P500 index since 1928



High UK, US vaccinations should limit hospitalisations



Source: Bloomberg, Our World in Data, Standard Chartered

Editorial

What to watch this summer

With Olympics excitement dampened by COVID-19 concerns, we are left with watching the next best thing this summer – the markets. History suggests the months of August-October are seasonally lacklustre for risk assets. We review some signposts that we believe will require a sharper-than-usual focus this summer:

a. The third wave and hospitalisations: New COVID-19 cases are rising globally, but we believe it is more pertinent to watch the ensuing hospitalisation rates. The UK is turning out to be a test case, given the resumption of normal activities this week – despite a surge in cases – following the inoculation of over half the adult population. Policymakers believe high vaccination rates should significantly reduce hospitalisations and fatality rates. They are preparing the public to live with COVID-19 as an endemic disease – just as the world has lived with influenza for decades. If the UK experiment works, it would support our preference for equities in markets with high vaccinations rates, such as the US and Europe. It is also likely to encourage other countries to accelerate the pace of vaccinations, enabling a faster global recovery.

b. Earnings season and full-year estimates: The US kicked off the Q2 season with solid earnings beats (with about a fifth of the S&P500 index companies reporting so far). The positive surprises have led to a rise in full-year 2021 earnings estimates (see page 4). This supports our long-held view that corporate earnings in the Developed Markets are likely to climb the 'wall of worry', beating estimates for the rest of the year as economic activity normalises alongside vaccinations. Equity returns should follow, while valuations ease.

c. Dovish turn in policy – Sustained accommodative policies are a major factor in our constructive view on markets. The ECB's formal shift this week to a policy that will target an average 2% inflation over the long-term enables the central bank to stay easy for longer. This move, which follows a similar shift by the Fed last year, is timely given the near-term headwinds from a potential third COVID-19 wave. In the US, concerns about peak y/y economic growth and the fiscal 'cliff' next year should give the Fed some space to delay the announcement of bond purchase tapering. At the US Congress last week, Fed Chair Powell pushed back notions that the Fed was about to start unwinding its accommodative policies. This raises the bar for the Fed to announce any tapering of bond purchases at next week's policy meeting. The Jackson Hole summit in August or the September policy meeting are more likely venues for a tapering discussion, with an announcement probably by the end of the year.

Meanwhile, the chances of further easing of China's monetary policy have risen with the recent cut in the bank reserve requirement. The State Council's recent direction to relax policy and revive infrastructure investment could herald further easing. Local governments have significant ammunition for investment, given that they have barely used up this year's quota for bond issuance.

The summer season ends with German elections in September. Any leftward turn in politics, especially with the Green party as a partner in a new government, could herald a structural shift in Germany's traditionally austere fiscal policies. This has the potential to lift Europe's long-term growth, risk assets and the EUR.

— Rajat Bhattacharya

The weekly macro balance sheet

Our weekly net assessment: On balance, we see the past week's data and policy as neutral for risk assets

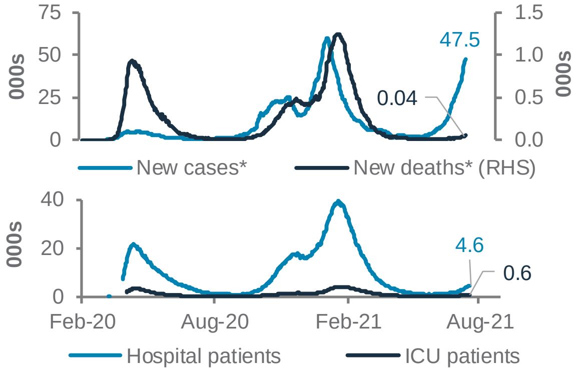
(+) factors: Supportive ECB policy, strong US retail sales

(-) factors: Rise in COVID cases, weak US, Euro area sentiment

	Positive for risk assets	Negative for risk assets
COVID-19	• Vaccinations continued to rise worldwide, led by China, where c. 1.5bn doses have been given • New cases continued to fall in Brazil and South Africa and stabilised near a 4-month low in India • President Biden said travel ban from Europe likely to be lifted soon; UK fully re-opened	• New cases continued to rise in the US, Europe, parts of Asia and other EMs; UK and Spain approached record highs • US said Delta variant made up over 80% of new cases; Japan reported cases among Olympic athletes • Vaccination pace slowing in the US and Europe
	Our assessment: Neutral – Rising vaccinations vs continued surge in Delta variant globally	
Macro data	• US retail sales rose unexpectedly; housing starts rose more than expected • Japan's exports rose more than expected • UK property sales rose to a record high in June; house price inflation slowed	• US Michigan consumer sentiment fell to a five-month low • US housing market index fell to an 11-month low • US weekly initial jobless claims unexpectedly rose • Euro area consumer confidence weakened more than expected
	Our assessment: Neutral – Strong US retail sales vs weakening US, Euro area consumer sentiment	
Policy developments	• ECB, adopting its new 2% average inflation policy target, said it plans to keep interest rates at record low levels for an extended period	• ECB loans survey showed a tightening of lending standards • BoJ downgraded Japan 2021 growth forecast to 3.8% from 4.0%
	Our assessment: Positive – New ECB policy portends extremely accommodative stance for a longer period	
Other developments		• EU rejected UK demand for a new post-Brexit deal on Northern Ireland
	Our assessment: Negative – Post-Brexit differences	

Hospitalisation and fatality rates in the UK remain subdued despite a surge in new cases

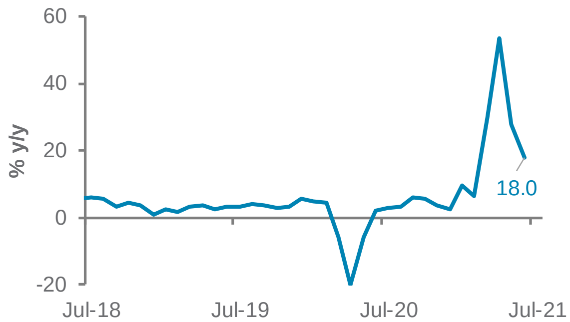
UK COVID-19 cases, hospitalisations & fatalities



Source: Our World in Data, Standard Chartered

US retail sales continue to surprise positively as consumers spend pandemic stimulus

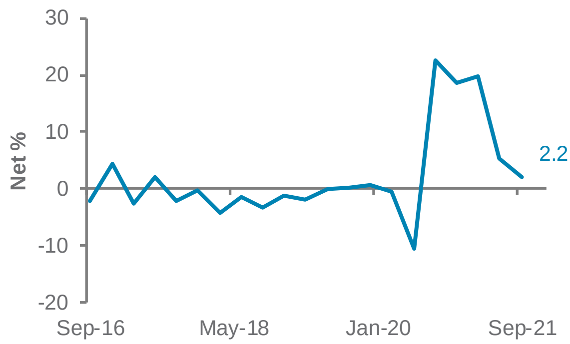
US retail sales growth



Source: Bloomberg, Standard Chartered

Euro area business lending outlook has weakened significantly in recent months – another reason for the ECB to stay easy

ECB survey showing expected change in lending to businesses



Source: Bloomberg, Standard Chartered

Top client questions

Are US equities at the start of a deeper correction?

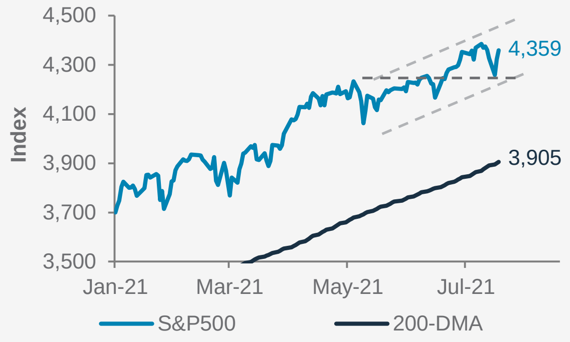
US equities were volatile at the start of the week, driven primarily by fears of a growth slowdown and a surge in new COVID-19 infections. However, we do not expect a deep correction in the market for now. On technical charts, US equities' uptrend looks intact. The S&P500's rebound from quite strong support at the May high of 4,238 signals this week's slide has not altered the structure of the uptrend. We are also in the midst of an earnings season, with positive surprises likely to halt any significant slide in the market.

21% of S&P500 companies have reported so far and Q2 earnings have surprised to the upside by 16%. The financial sector is most advanced in reporting earnings, with 46% of companies having reported with an earnings surprise of 23%. For the market overall, consensus 2021 earnings growth has risen from 37% at the start of July to 40%. While this rising 2021 base has brought the 2022 growth estimate down slightly from 12% at the start of July to 11%, combined earnings estimates for 2021 and 2022 have gone up. This supports our preferred view of US equities.

— **Manish Jaradi,** *Senior Investment Strategist*
— **Fook Hien Yap,** *Senior Investment Strategist*

The US equity uptrend appears intact from the charts; we do not see a deep correction

S&P500 index



Source: Bloomberg, Standard Chartered

What are the implications of China's required reserve ratio (RRR) cut on its equity and bond markets?

The People's Bank of China's (PBoC) RRR cut last week is a positive step in terms of supporting growth, particularly since the central bank has never stopped at just one RRR cut in prior cycles. While we do not expect the easing to immediately reverse what still appears to be a slowing economy, it does highlight that authorities are shifting their priority from curbing 'excessive' credit to stabilising growth. This should eventually support sentiment and market liquidity.

Cuts in reserve requirements have historically marked the bottom of the credit cycle, but they do not signal an imminent rise in equity markets. While earnings revision trends have regained some positive momentum, signs of further policy easing, especially in regulatory policies, and renewed CNY appreciation are likely needed before we can consider turning more constructive on Chinese equities. However, Asian USD-denominated bonds may represent an attractive route to gain exposure to China at this point given valuations in this asset class have eased considerably, particularly when compared to Developed Market corporate bonds.

— **DJ Cheong, CFA,** *Investment Strategist*

There is usually some lag between China's first RRR cut and subsequent equity gains

12-month net change in China's bank reserve requirements vs. 12-month rolling MSCI China index returns

Source: Bloomberg, Standard Chartered

Top client questions (cont'd)

What are the implications of the stress in China real estate sector on Asia USD bonds?

In recent weeks, China's property sector has been under increased scrutiny as regulatory pressures on a large developer resulted in softer sentiment and underperformance of the sector's USD bonds.

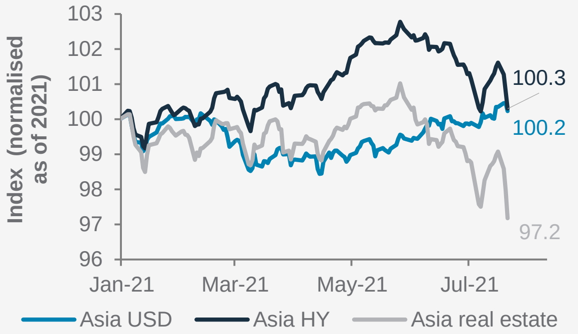
In our view, it is important to differentiate the short- and long-term impact of the regulatory scrutiny around China's 3 Red Lines (3RL) policy. In the near term, we believe the underperformance of developers that stack up poorly on the 3RL policy is likely to extend. Idiosyncratic defaults and heightened volatility are likely as well. However, from a longer-term perspective, we view the 3RL policy as a positive as it pushes an increasing number of property developers to strengthen their balance sheets, improving overall sector credit quality.

While we cannot rule out further underperformance of Asia HY bonds over the coming few months, due to property sector concerns, we believe valuations have become increasingly attractive relative to Asia Investment Grade and even US HY bonds. Hence, we would consider any further weakness as an opportunity to add exposure to Asia HY bonds.

— **Abhilash Narayan,** *Senior Investment Strategist*

We believe valuations in Asia High Yield bonds are looking increasingly attractive vs. Investment Grade peers after recent declines

Performance of Asia USD, Asia HY and Asia real estate sector bond indices



Source: Bloomberg, Standard Chartered

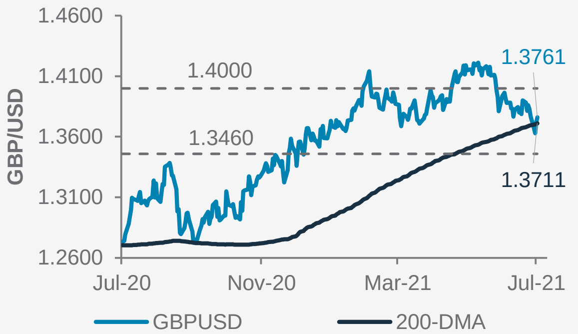
Will Britain (and the GBP) lead the way out of the pandemic?

The sight of 130,000 fans attending the British Grand Prix and 30,000 strolling around The Open golf course suggests that the UK may provide the roadmap for global growth and USD direction in H2. If their "vaccinate and live with it" COVID-19 strategy leads to a rise in cases but relatively low hospitalisation rates, other countries will likely follow suit. Global growth should transition from recovery to expansion, the counter-cyclical USD could fall and the GBP, alongside other pro-risk currencies, could rally strongly. If the strategy fails, then it is likely that the global recovery stalls, the USD rises and the GBP slides.

The transition phase could see two-way volatility through the remaining summer weeks. UK hospitalisation and mortality rates will be key to determining which scenario is playing out. Investors are likely to shuttle between fear and hope, but we expect the strategy will succeed. GBP/USD is pivoting around the key 1.3650-1.3700 level. Any short-term dips should see support around 1.3460 and then 1.3280. A break above 1.39 and then 1.40 likely signals a rally to test three-year highs around 1.44.

The GBP has technical support around 1.3650, followed by 1.3460 and 1.3280

GBP/USD



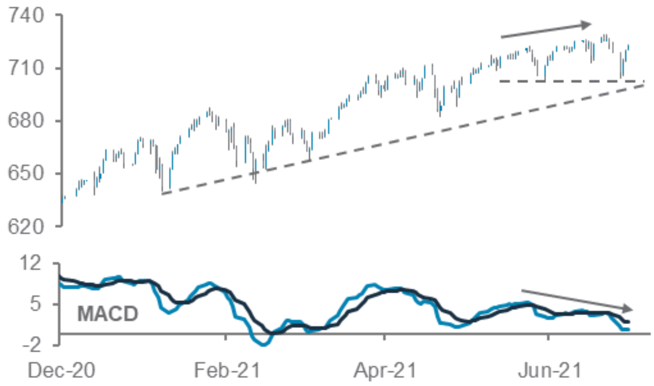
Source: Bloomberg, Standard Chartered

Technical charts of the week

Manish Jaradi
Senior Investment Strategist

Global equities: Correction imminent?

MSCI All Country World index daily chart with Moving Average Convergence Divergence indicator (MACD)

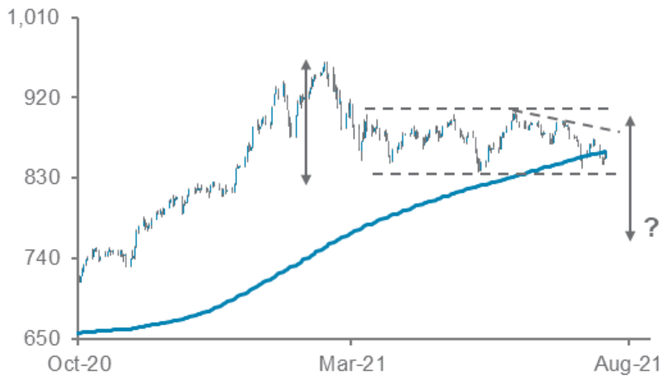


Source: Refinitiv, Standard Chartered

> There are some signs of trend deceleration in the short term, but not enough to suggest an imminent correction. The index would need to break below immediate support at the June low of 703 for the upward pressure to fade.

Asian equities: Looking vulnerable

MSCI Asia ex-Japan index daily chart with 200-DMA

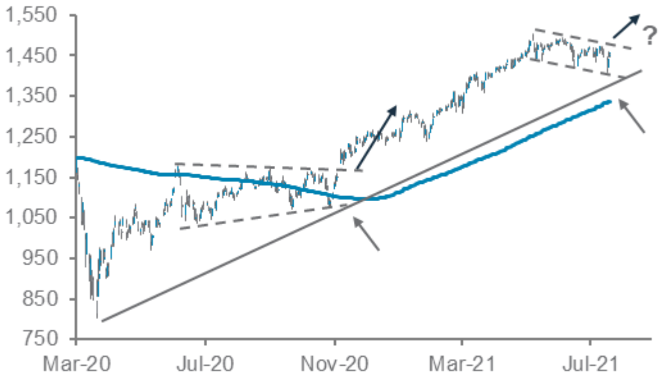


Source: Bloomberg, Standard Chartered

> The longer the MSCI Asia ex-Japan index stays in the range, the more vulnerable it could get to another leg lower. For the downward pressure from June to ease, at a minimum, the index needs to break above a minor downtrend line from June (now at about 883).

S&P500 Value: A short-term pause

S&P500 Value index daily chart with 200-DMA

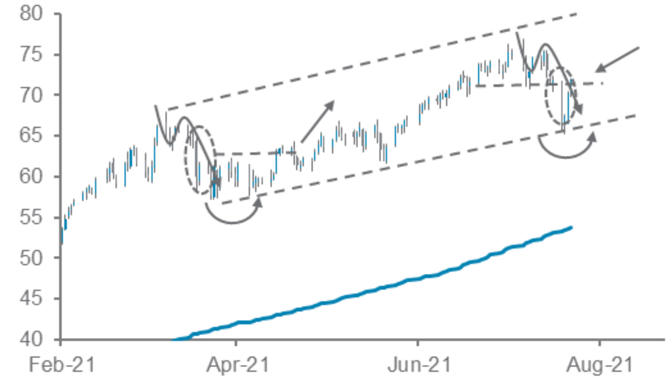


Source: Bloomberg, Standard Chartered

> The recent consolidation is similar to that of mid-2020. The key difference is that last year it was below the 200-DMA, whereas now it is firmly above the average. The rising long-term average is a sign that the broader trend is up.

Crude oil: Still within its defined uptrend

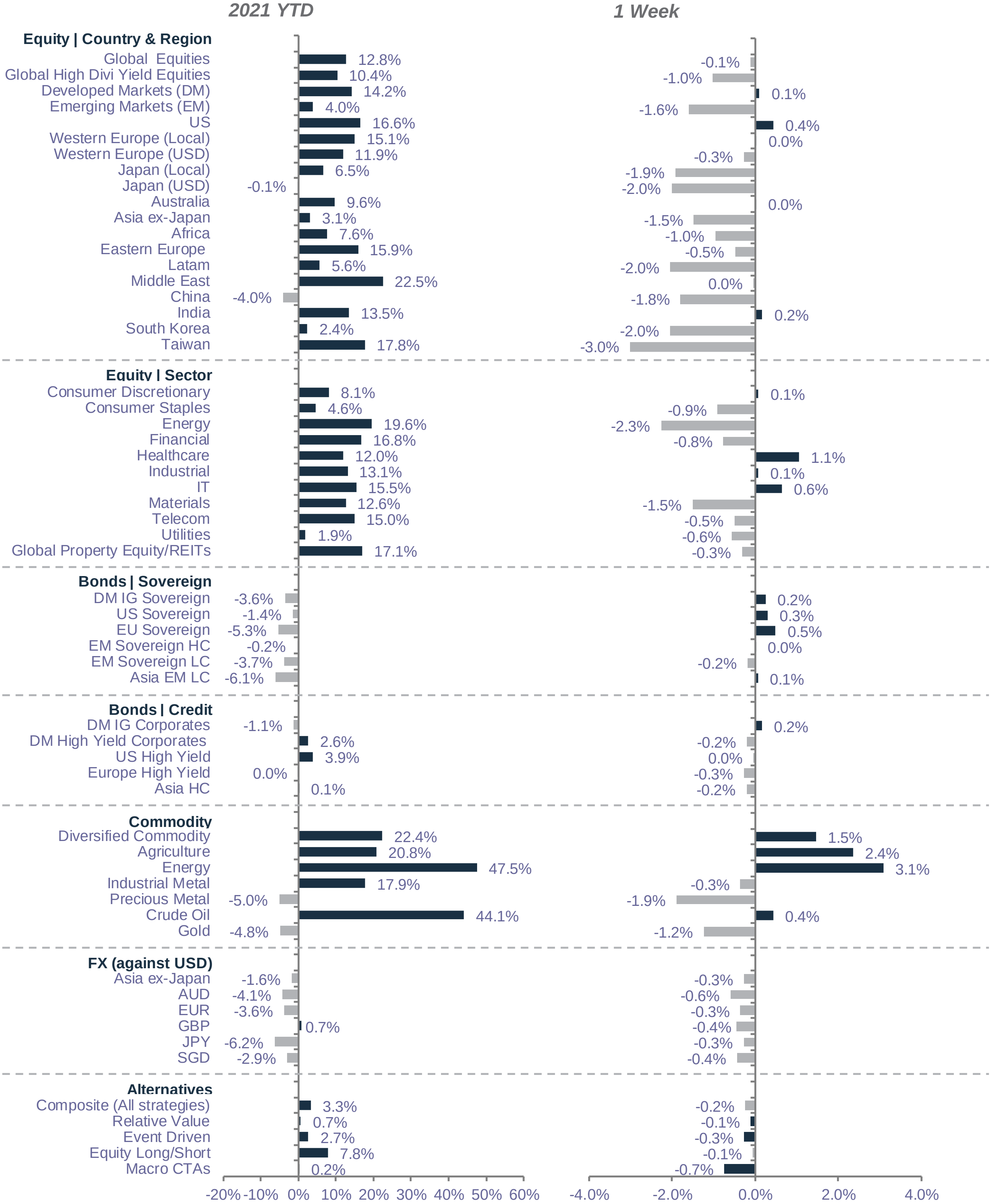
WTI Crude Oil Futures continuous contract daily chart with 200-DMA



Source: Refinitiv, Standard Chartered

> This week's decline looks more like a pause, than a reversal – at least yet. The move is similar to the one in Q1 -- a three-leg-move lower. Still, oil needs to break decisively above 70.75 for the uptrend to continue.

Market performance summary*



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

*Performance in USD terms unless otherwise stated, 2021 YTD performance from 31 December 2020 to 22 July 2021; 1-week period: 15 July 2021 to 22 July 2021

Our asset class views at a glance

Asset class			
Equities	▲	**Alternatives**	◆
Euro area	▲	Equity hedge	▲
UK	▲	Event-driven	▲
US	▲	Relative value	▼
Asia ex-Japan	◆	Global macro	◆
Japan	▼		
Other EM	◆	**Cash**	▼
		USD	▼
Bonds (Credit)	◆	EUR	▲
Asia USD	▲	GBP	▲
Corp DM HY	▲	AUD	▲
Govt EM USD	▲	CNY	◆
Corp DM IG	▼	JPY	◆
Bonds (Govt)	▼	**Gold**	◆
Govt EM Local	◆		
Govt DM IG	▼		

Source: Standard Chartered Global Investment Committee

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

Economic and market calendar

	Event	Next week	Period	Prior
MON	GE	IFO Expectations	Jul	104
	US	New Home Sales	Jun	769k
TUE	CH	Industrial Profits y/y	Jun	36.4%
WED				
THUR	US	FOMC Rate Decision	28-Jul	0.3%
	EC	Economic Confidence	Jul	117.9
	GE	CPI EU Harmonized y/y	Jul P	2.1%
FRI/SAT	US	PCE Deflator y/y	Jun	3.9%
	US	PCE Core Deflator y/y	Jun	3.4%
	JN	Industrial Production y/y	Jun P	21.1%
	EC	Unemployment Rate	Jun	7.9%

Source: Bloomberg, Standard Chartered
Prior 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

S&P500 has first support 1.6% below current level

Technical indicators for key markets as on 22 July 2021

Index	Spot	1st support	1st resistance
S&P500	4,367	4,295	4,404
STOXX 50	4,059	3,972	4,103
FTSE 100	6,968	6,872	7,036
Nikkei 225	27,548	27,290	27,905
Shanghai Comp	3,575	3,549	3,587
Hang Seng	27,724	27,297	28,077
MSCI Asia ex-Japan	860	850	869
MSCI EM	1,326	1,312	1,341
Brent (ICE)	73.8	70.3	75.5
Gold	1,807	1,803	1,812
UST 10Y Yield	1.28	1.21	1.32

Source: Bloomberg, Standard Chartered

Investor diversity has normalised across assets

Our proprietary market diversity indicators as of 21 July

Level 1	Diversity	1-month trend	Fractal dimension
Global Bonds	●	↑	1.82
Global Equities	●	↑	1.57
Gold	●	↑	1.95
Equity			
MSCI US	◐	→	1.48
MSCI Europe	◐	↑	1.50
MSCI AC AXJ	●	↑	1.60
Fixed Income			
DM Corp Bond	●	→	1.50
DM High Yield	●	↑	1.51
EM USD	◐	→	1.46
EM Local	●	↑	2.13
Asia USD	●	↑	1.56
Currencies			
EUR/USD	◐	→	1.49

Source: Bloomberg, Standard Chartered; **Fractal dimensions below 1.25 indicate extremely low market diversity/high risk of a reversal**

Legend: ● High | ◐ Low to mid | ○ Critically low

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