



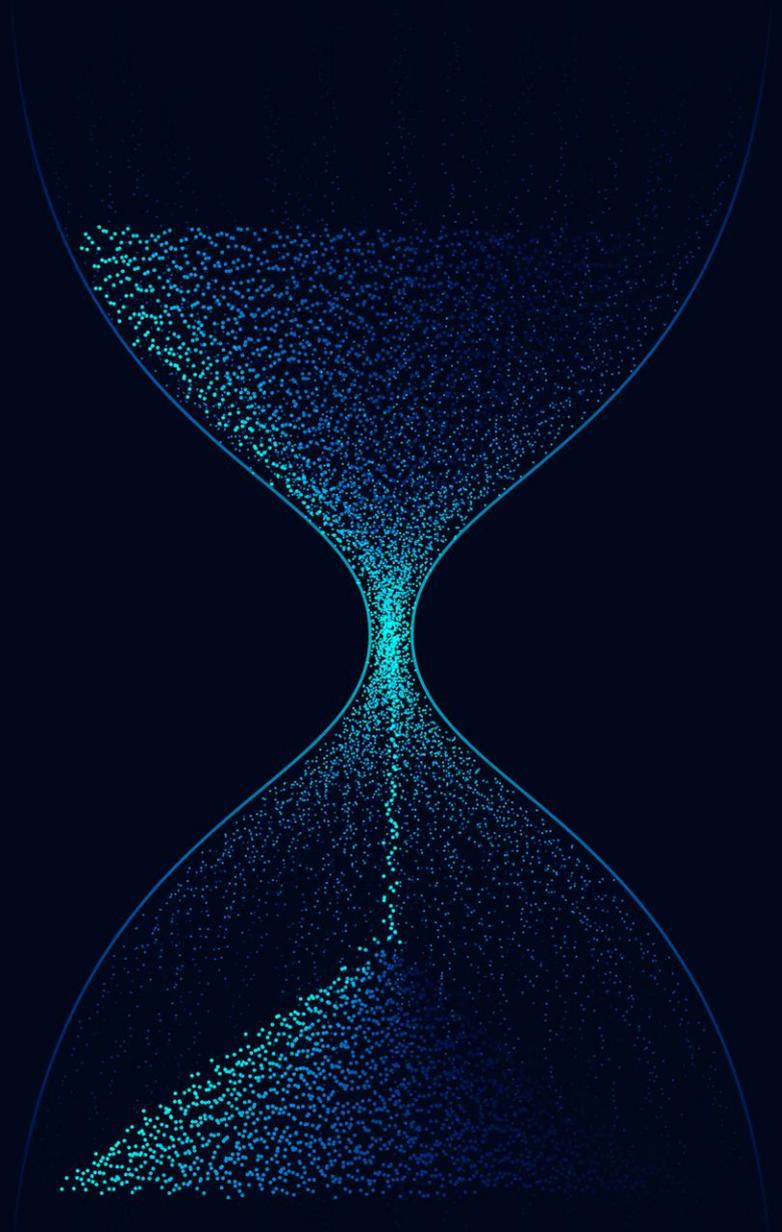
Global Market Outlook

Living with COVID?

We see equity markets transitioning to a slower, but more sustainable, pace of gains as countries vaccinate and learn to live with COVID-19. US and European equities remain preferred. We view Asia ex-Japan and China equities as core holdings, but await more attractive entry levels.

Markets are likely to focus on the timing of Fed tapering of bond purchases, China's policy direction, inflation expectations and the effectiveness of COVID-19 'vaccinate-and-normalise' strategies.

We expect gradually higher US bond yields once excessively bearish Treasury positioning eases as growth remains well-supported. Gradually rising Treasury yields would not alter our weak USD view and preference for riskier bonds.



What to make of China's regulatory crackdown in recent months?

Are there opportunities amid China's ESG ambitions?

What is the technical outlook for China stocks and US Treasury yields?

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Investment strategy and key themes

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Investor implications on a 12-month horizon

- Global equities over bonds and cash
- In equities: US, Euro area, UK favoured
- In bonds: DM HY, Asia USD, EM USD preferred
- In FX: USD likely to fall against EUR, GBP, AUD, CAD, NZD

Key themes

- Ready, Steady, Rotate
- Race for Income
- USD to slump in 2021
- Disruptive Innovation
- Climate change
- A world of yield-free risk

Living with COVID?

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- We expect gradually higher US bond yields once excessively bearish Treasury positioning eases as growth remains well-supported. Gradually rising Treasury yields would not alter our weak USD view and preference for riskier bonds.

Shifting to slower, but sustainable, pace of returns

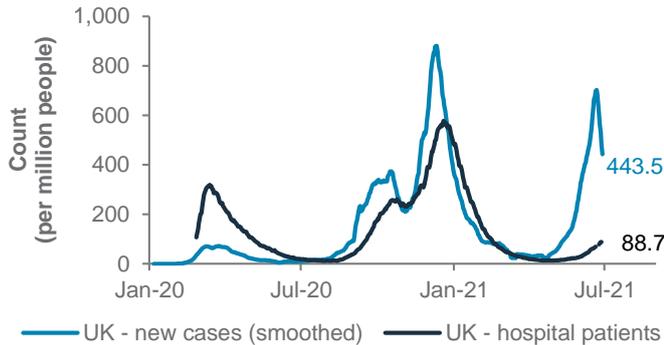
Since we published our H2 Outlook, most asset classes have been relatively rangebound, with US government (Treasury) yields (which fell 22bps since end-June) and Chinese equities (down 12.7%) being the two notable exceptions. The market narrative is likely to be increasingly focused on (i) how 'learning to live with COVID-19' strategies fare, (ii) topping out of inflation expectations, (iii) how soon the Fed signals tapering of bond purchases, and (iv) China's policy path. In our assessment, these factors remain consistent with a somewhat slower, but more sustainable, pace of equity market gains, accompanied by a higher level of volatility.

From Alpha to Delta

There are concerns that the sharp rise in the Delta variant of COVID-19 could lead to yet another pause in economic recovery as infections rebound amid an incomplete vaccination process. The UK, though, may offer the best gauge of how this could pan out. UK infections appear to have peaked already; if the surge earlier is not accompanied by a similarly sharp rise in hospitalisation rates, fears of further restrictions could reduce significantly. Alternatively, a relapse to increased mobility restrictions could disappoint markets, though this is likely to be short-lived, given how households, businesses and markets have adapted to the pandemic.

Fig. 1 UK reopening ‘experiment’ could brighten outlook if hospitalisations remain contained

UK COVID cases, hospitalisation (7-day rolling average)



Source: Our World in Data, Standard Chartered

The uncertainty is likely feeding into bond yields – while falling inflation expectations partly explain the decline in yields, growth concerns are visible in lower real (net-of-inflation) yields. An incomplete unwind of excessively bearish Treasury positions is also likely a factor, a normalisation of which is eventually likely to see a renewed rebound in yields as growth concerns recede.

Any Fed signalling on the timing and pace of tapering of bond purchases is also likely to support higher bond yields, possibly accompanied by temporary equity volatility. We continue to expect tapering to only start in early 2022, with an announcement later this year.

In China, regulatory policy continues to tighten for specific industries. However, recent signals (including the PBoC’s bank reserve ratio cut) shows authorities are starting to worry more about the growth outlook, potentially setting the stage for further policy easing.

Looking past peak rebound

For global equities, we believe these factors support our view of a return to a slower, but more sustainable, pace of gains, albeit accompanied by somewhat higher volatility compared with earlier this year.

Fig. 3 August-October is seasonally lacklustre for equity markets

3m average rolling returns of S&P500 since 1928



Source: Bloomberg, Standard Chartered

Fig. 2 The pullback in inflation expectations is one factor behind lower US Treasury yields

US 10-year Treasury yield and inflation expectations



Source: Bloomberg, Standard Chartered

Our preference for equities in Europe (including the UK) remains unchanged. How hospitalisation rates play out will likely be key, but we expect any bouts of volatility to be transitory unless governments are forced into imposing significant new restrictions on economic activity. We similarly maintain our preference for the US. While we may be past the peak of the earnings growth recovery, consensus data supports our view that earnings (and hence markets) are likely to settle into a slower, but more sustainable, pace of growth.

However, Asian equities face headwinds from Chinese policy. Historically, the PBoC’s cuts in banks’ required reserve ratio (RRR) have supported equity markets with a long lag. Meanwhile, regulatory policies continue to tighten and equity market technicals remain weak. We continue to see China and Asia ex-Japan equities as core holdings, but await more attractive entry levels.

Bad for you is good for me

Higher US Treasury yields usually act as a headwind for most bond asset classes (higher yields translate to lower prices). However, we remain comfortable with our preference for riskier bonds.

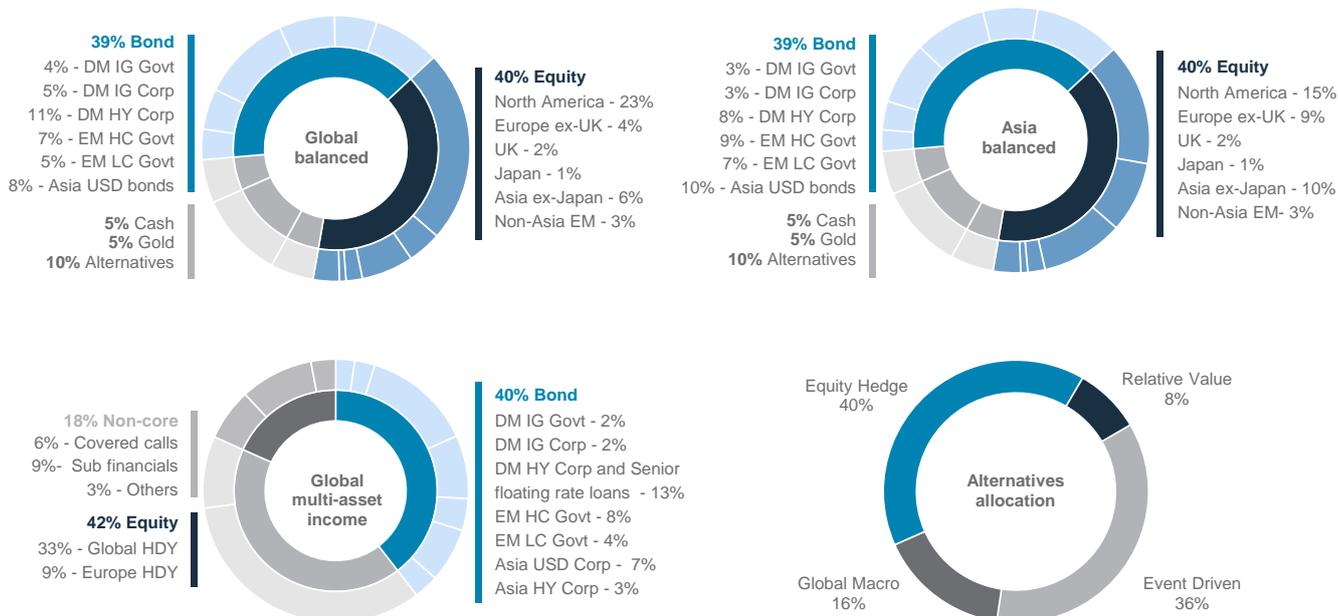
Asia USD bonds arguably offer an attractive combination of a valuation buffer and relatively low sensitivity to Treasury yields. Tightening regulatory policies in China remain a headwind, though we believe this is less of a risk to USD bonds (given the policies should eventually improve credit quality), than for equities (tighter regulations can impact future growth).

Higher yielding bonds in Developed Markets (DM) have relatively low sensitivity to US government bond yields. Although Emerging Market (EM) USD bonds are more sensitive, we believe comfortable valuations offer a sufficient buffer.

A recovery in risk appetite and broadening of growth across the globe should support non-US yields, also triggering a reversal in the recent USD strength.

Our 12-month tactical asset allocation

12-month tactical asset allocations for investors with a moderate risk profile (numbers may not sum to 100% due to rounding)



Summary of our key asset class views

View	Detail
USD cash	▼ + Safety - Close to no yield
Bonds	
<i>DM Govt</i>	▼ + High credit quality, policy support - Very sensitive to rising US bond yields
<i>DM IG Corporate</i>	▼ + Policy support - Very sensitive to rising US bond yields
<i>DM HY Corporate</i>	▲ + Attractive yield, low rate sensitivity - Valuations, risk of rising defaults
<i>EM USD Govt</i>	▲ + Attractive yield, attractive value - Sensitivity to rising yields, USD rebound
<i>EM Local Ccy Govt</i>	◆ + Moderate yield, weak USD view - Rising policy rates in some EMs
<i>Asia USD</i>	▲ + Moderate yield, low volatility - China policy, default contagion
Equities	
<i>North America</i>	▲ + Growth, earnings rebound, policy support - Early Fed taper, potential tax rise
<i>Europe ex-UK</i>	▲ + Vaccinations, Value rotation, policy support - Renewed COVID-19 wave
<i>UK</i>	▲ + Attractive valuation, value rotation, Brexit deal - Policy risk, strong GBP
<i>Japan</i>	▼ + Global economic recovery - China policy, structural deflation
<i>Asia ex-Japan</i>	◆ + Earnings rebound - China policy, COVID-19 risk, USD rebound
Gold	◆ + Weak USD, equity vol - Treasury yield rebound, Return of risk appetite
Alternatives	◆ + Diversifier characteristics - Equity, corporate bond volatility

Source: Standard Chartered Global Investment Committee

Legend: ▲ Most preferred | ▼ Least preferred | ◆ Core holding || Green: upgrade from prior view | Red: downgrade from prior view

Perspectives on key client questions

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Q What to make of China's regulatory crackdown?

Chinese authorities have issued a series of regulatory reforms across internet, fintech, healthcare and education sectors in recent months. These moves have rattled investors, negatively impacting China's financial markets. The MSCI Asia ex-Japan index is down 12.5% since its peak in February, dragged by China (-10.8% YTD), which makes up 43% of the index. In bonds, Asia USD bonds returned -0.5% this year, outperforming Developed Market Investment Grade (IG) corporate bonds (-0.7%).

Regulatory uncertainties likely to remain an overhang

There are many questions about the motivations behind this crackdown and which sectors may be targeted next. In our view, there remains considerable uncertainty, but the measures announced so far seem to be aimed at advancing China's long-term strategic objectives e.g. to achieve common prosperity, global leadership in technology (high-tech manufacturing, rather than consumer tech) and managing competition with the US. For example, the guidance for companies to pay minimum wage and enhance social benefits to flexible workers are likely aimed at enhancing social equality. Similarly, the crackdown on internet companies may encourage more domestic firms to list in China or HK, helping to develop domestic capital markets, thus supporting China's long-term competition with the US.

We review the 2014-2016 anti-corruption campaign against Macau's gaming sector, when affected stocks underperformed the Hang Seng Index (HSI) by more than 50%. While Chinese internet and property sectors are currently under pressure (Fig. 5), they are of greater strategic importance than casinos/gaming. Moreover, revenue growth, especially in the internet sector, is likely to be an additional pillar of support.

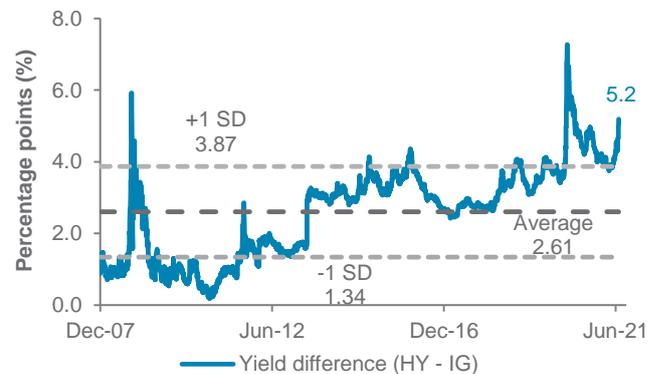


Fig. 4 Chinese (offshore) equities have suffered the brunt of the regulatory pressures. We prefer Asia USD bonds, particularly higher yielding debt, to build exposure to Chinese assets for now

Select indexes rebased to 100 on 31-Dec-2020



Yield difference between Asia IG and HY USD bonds

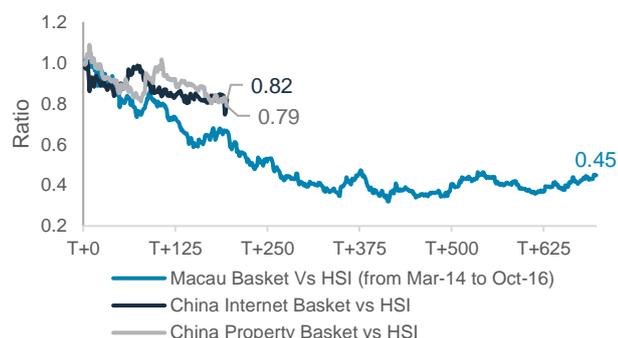


Source: MSCI, JP Morgan, Bloomberg, Standard Chartered; As of 26-Jul-2021. Rebased to 100 = 31-Dec-2020
SD = Standard Deviation

While the education sector is much smaller in terms of market capitalisation (comprising less than 1% and 1-2% of the broader MSCI China index and the consumer discretionary sector, respectively), the recent reforms do raise the question of which sectors may be at risk next. Sectors seen to exacerbate social inequality or obstruct policy goals may possibly be at risk.

Fig. 5 The sell-off in China's technology, real estate sectors has been much shallower since the regulatory moves vs Macau gaming in 2014-2016

Performance of sector baskets* relative to Hang Seng Index since the onset of regulatory moves (T = days)



Source: Bloomberg, Standard Chartered; As of 26-Jul-2021

* Each basket consists of equally weighted HK-listed stocks that provide an approximate sector representation: 1) Macau: Galaxy, Sands, 2) China internet: Tencent, Alibaba, JD.com, NetEase, 3) China property: COLI, CR Land, Vanke, Country Garden.

Monetary policy turning more supportive

We believe regulatory pressure will likely remain an overhang for equity markets near term, but the cut in bank reserve requirement ratio (RRR), is a step in a positive direction. Historically, the PBOC has never stopped with just one RRR cut. Thus, further easing can be expected. Easing monetary policies could signal the bottoming of China's credit impulse and offer tailwinds to equities – albeit with a lag. However, that alone is unlikely to ease pressure on China equities near term. Although earnings revisions have regained positive momentum, we would watch for signs of further policy easing, especially on the regulatory front.

Overall, we expect China onshore and offshore equities to perform broadly in line with Asia ex-Japan equities over the next 6-12 months. Within China equities, we prefer the industrial and energy sectors that are less impacted by domestic policies and are driven by the global economic expansion cycle. Some Chinese sub-sectors supporting long term policy goals, such as electric vehicles (EVs) or semiconductors, remain attractive routes for adding long-term exposure, in our view. Moreover, these sectors are two key pillars of our structural *Disruptive Innovation* theme.

Technicals at key long-term support

The MSCI China index is testing crucial support on the upward sloping 200-week moving average. Any rebound from here raises the probability of a rebound as it did in 2018, providing a decent entry for long-term investors. In addition, if the intensity and tone of regulators soften over the coming months, this may create buying opportunities in selective sectors, given valuations have eased considerably. We would look for signs of bottoming technicals before considering turning more constructive on the Chinese equities, which remain a core holding. See page 14 for our technical commentary.

Attractive valuations, defensive character work in favour of China USD bonds

Apart from select equity sectors that are likely to benefit from targeted government policies and the ongoing global economic expansion, we believe USD-denominated corporate bonds are a more attractive route for taking exposure in China.

Asia USD bonds remain one of our preferred areas, given improving corporate sector profitability, contained defaults, low volatility and attractive valuations compared with US corporate bonds. The PBoC's RRR cut should help ease access to credit for Chinese issuers. This should help improve onshore liquidity via improved supply of onshore financing, thus potentially supporting bond prices.

Nevertheless, in recent weeks, China's property sector has been under increased scrutiny as regulatory pressures on a large developer resulted in weaker 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, especially in terms of China's 3 Red Lines (3RL) policy that seeks to improve the balance sheet health of property developers.

In the near term, we believe the underperformance of developers that stack up poorly against the 3RL policy objectives is likely to extend. Idiosyncratic defaults and heightened volatility are likely. However, from a longer-term perspective, we view the 3RL policy as positive as it pushes an increasing number of developers to strengthen their balance sheets, improving overall sector credit quality.

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

China's ESG ambitions offer investment opportunities

China's sustainable development aspirations

Over the past few years, China has undertaken several environmental protection measures as it seeks to establish leadership in sustainable development. Key announcements related to this topic have been aimed at achieving ambitious targets of reaching a carbon emission peak by 2030 and carbon neutrality by 2060.

While we await further details and actions, we believe setting the ambitious targets is an important first step. It shows that emissions reduction and protection and restoration of ecosystems are a core focus of China's 14th Five Year Plan (FYP).

China's FYP is a key policy document that establishes the country's medium-term goals towards social and economic development and helps orchestrate and accelerate progress in identified areas. For instance, the 13th FYP had a strong focus on reducing pollution levels and this saw PM2.5 levels in the Beijing-Tianjin-Hebei region drop by 36%. This also resulted in a reduction of coal usage in the primary energy mix from 63.7% in 2015 to 56.8% in 2020.

Key policy and regulatory developments

Sustainable finance is critical to the promotion of sustainable development. Here, the 2016 guidelines laid the foundation for a sustainable financial system in China. These reforms have trickled into the way Chinese businesses are conducted.

This year has seen more announcements to promote sustainable finance and development:

Fig. 6 2021 - key announcements

- Q1**
- China's State Council releases guidelines to accelerate the building of a green and low-carbon circular economic system
 - Details of China's Carbon Emission Trading system announced in February
 - China's first green finance regulation in Shenzhen takes effect in March, requiring financial institutions to disclose information on their environmental impact
 - Targets for carbon emissions reduction and accelerating green development a focus during the Two Sessions (Beijing's annual parliamentary meetings)

Q2

- 2021 catalogue for green bonds to exclude fossil fuel-related projects
- PBoC Shanghai meets with Chinese and foreign banks to discuss how to further develop carbon finance
- Plans to create a fund to manage carbon credit sales income announced in Shenzhen
- China Securities Regulatory Commission (CSRC) issues revised guidelines requiring listed companies to disclose environmental, social data

July

- The National Emissions Trading Scheme (ETS) officially started on 16 July

Source: Government announcements, media reports, Standard Chartered

Importance of ESG reporting and disclosures in attracting global investment capital

One important outcome of the recent policy and regulatory announcements, besides supporting the development of bond and carbon markets, will be improved ESG data disclosures driven by CSRC's ESG reporting requirements announced in June.

With CSRC's revised guidelines on the format of annual and semi-annual reports, listed companies are now required to disclose environmental and social data in greater detail, especially around the measures taken to reduce carbon emissions during the period and the outcome of the efforts.

Fig. 7 ESG reporting has increased in China

ESG reporting of CSI 300 A-shares companies



Source: Ping An Digital Economic Research Centre, Standard Chartered

This data disclosure is important in attracting global investments into Chinese companies. International investors have previously found it challenging to make ESG-themed investments in China due to inadequate data for assessing companies' ESG performance. This is changing, with 85% of CSI 300 A-shares companies releasing ESG disclosures, matching the 90% rate among S&P companies. This is a good start, though more needs to be done in developing quality reporting as only a small proportion of these releases are audited.

What does this mean for investors?

Significant risks for ESG laggards, especially in climate progress and data disclosures

We expect increased pressure on reporting material ESG data, with continued efforts by the PBoC to standardise mandatory environmental information disclosure requirements. Companies that are laggards in this area face both regulatory and reputational risks.

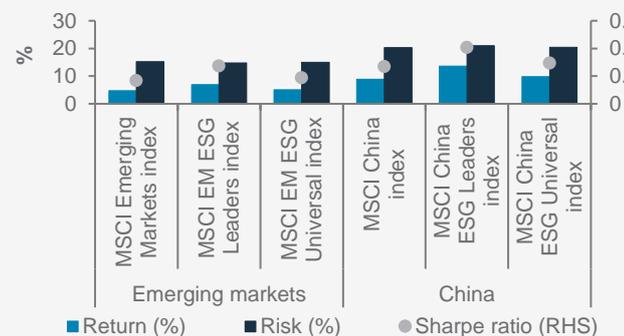
The launch of China's long-anticipated ETS will force carbon-intensive companies to cut pollution or face potential economic/financial risks. While the ETS initially only covers power and heat generation, which accounts for 40% of China's emissions, plans are under way to eventually include power generation, steel, cement and other key industrial sectors.

Capturing alpha by identifying leaders in ESG

An analysis on EM and China equity markets by the Principles for Responsible Investing (PRI) helps highlight the potential value of ESG within a portfolio.

Fig. 8 ESG portfolios delivered stronger risk-adjusted returns relative to broader markets

EM and China equity risk & returns from 2013 to 2019



Source: Principles for Responsible Investment, Standard Chartered

Their analysis suggests portfolios with superior ESG characteristics are able to deliver alpha, while offering relatively lower downside risk compared with broader markets. Between EM and China equity markets, the ESG factor's alpha generation capability in China equities was also higher than that of EMs.

Thematic opportunities in addressing climate change remain attractive in the long term

China's focus on achieving carbon neutrality by 2060 could create significant investment opportunities related to ecological protection and a low-carbon transition. China has already invested twice as much as the US on climate action to date, strengthening its solar energy capacity to nearly triple that of the US last year. In 2020, the Chinese government launched the National Green Development Fund, a state-run private equity fund currently worth USD 13.6bn, focusing on investing in green projects and firms.

Fig. 9 Sales of Chinese green bonds have reached a record in 2021

Issuance of green bonds from 2015 to 2021



Source: Bloomberg, Standard Chartered

While capital flows into ESG-related ETFs rose more than five-fold between 2018 and 2019, a total of 11 new fund launches were recorded in 2020. Sale of China's green bonds also reached new highs in 2021, with proceeds going to green projects. While sudden policy shifts are a risk, valuations of Chinese 'green' stocks – trading on par with that of Euro area ESG leaders (12-month forward P/E of 16.3x vs 17.8x) – remain healthy.

Since committing to carbon neutrality, China has incorporated climate protection measures, aligning more closely with the global environmental agenda. It continues to dominate the production of EV batteries and solar panels globally. We remain optimistic about growth and investment opportunities in this space.

Fig. 10 Valuations of China ESG leaders are on par with EU counterparts

12-month forward P/E ratios of US, EU, China ESG stocks



Source: Bloomberg, Standard Chartered

Macro overview – at a glance

Rajat Bhattacharya
Senior Investment Strategist



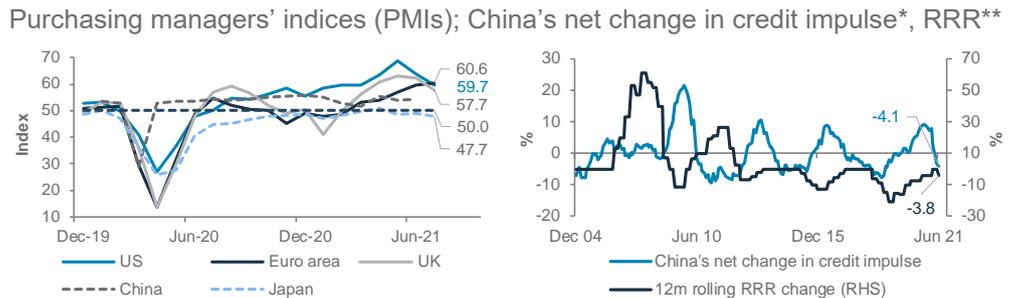
Key themes

We expect the global recovery to continue as major economies, such as the US, Europe and China, achieve ‘herd immunity’ against COVID-19 in Q3 through high levels of vaccinations, enabling them to resume normal business activity. Growth in the US and Europe is likely to remain firmly above pre-pandemic trend well into 2022, despite a moderation in the pace after this year’s bounce back. China is the only major economy that is likely to have slower growth in 2022 vs pre-pandemic levels, but we see the PBoC’s cut in RRR as the start of a credit easing cycle, which should help stabilise growth. We also expect monetary policies to remain accommodative in major economies, offsetting fiscal policy tightening (most significantly in the US). The ECB’s latest policy shift will enable it tolerate inflation above 2% for a while, implying that policy is likely to stay easy for longer. In the US, the current surge in inflation is likely to be transitory as supply bottlenecks and labour market distortions fade by Q4. Inflation expectations have also softened. This should allow the Fed to delay tapering of bond purchases until early 2022.

Key chart

Business confidence in major economies remains strong, despite moderating from very high levels. This supports our view of robust economic growth as countries re-open and monetary policies remain highly accommodative

Fig. 11 Global business confidence still robust; China starts to ease policy



Source: Bloomberg, Standard Chartered; *Change in credit as % of GDP; **Bank required reserve ratio

Macro factors positive for risk assets

Macro factors negative for risk assets

Country	Policy Direction	Positive Factors	Negative Factors
US	▼ ◆ ▲	+ Herd immunity in Q3; above-trend growth + Savings, jobs rebound to lift consumption + Business spending, infrastructure boost + Fed rate on hold; still-high fiscal support	– Proposed tax hikes, fiscal drag from 2022 – COVID mutations; precautionary savings – Slowing goods demand; supply bottleneck – Weak lending; Fed to taper bond buying
Euro area	▼ ◆ △	+ Herd immunity in Q3; above-trend growth + H2 consumption lift; industry robust + ECB easy; Recovery Fund pay-out in H2	– COVID variant risk; slowing vaccinations – Precautionary savings; high jobless rate – Industry supply constraints; fund delays
China	▼ ◆ △	+ Herd immunity in Q3 to lift consumption + Strong industry, exports; infrastructure lift + PBoC policy easing to support growth	– Global goods-to-service shift to hit exports – Regulatory tightening; rising input costs – Precautionary savings; geopolitical risk
Japan	▼ ◆ △	+ Strong export growth, pent-up demand + Vaccination rates to improve in H2 + More fiscal stimulus likely amid slowdown	– Global goods-to-service shift to hit exports – Precautionary savings; COVID variants – Structural deflationary forces
UK	▼ ◆ △	+ Herd immunity in Q3; above-trend growth + H2 consumption lift; longer pandemic aid + Infrastructure boost; easing Scottish risk	– COVID variant risk; precautionary savings – Brexit-related supply chain disruptions – High inflation risks tighter monetary policy

Source: Standard Chartered Global Investment Committee

Legend: ▲ Tighter policy | ▼ Easier policy | ◆ Neutral policy

Bonds – at a glance

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Key themes

We believe long term US Treasury yields have overshot fundamentals following the latest decline, driven by growth slowdown concerns, fall in inflation expectations and resurgence in virus cases. Additionally, real yields (yields net of inflation) are close to multi-decade lows. We expect real yields to rebound, driven by a rise in the 10-year US Treasury yield to a 1.75%-2.0% range over the next 12 months. Thus, we favour higher yielding and lower maturity bonds, such as DM HY bonds, Asian USD bonds and EM USD government bonds, which should benefit from stronger economic growth. We believe the recent rise in Asian HY spreads, especially for B-rated bonds, provide attractive risk-reward, despite increased regulatory scrutiny around the technology and property sectors in China.

Key chart

10-year US Treasury yield to rise to 1.75%-2.0% over the next 12 months, leading to higher real yields; Asia HY bonds offer an attractive pick-up over Asia IG bonds, with the spread ratio close to record highs

Fig. 12 US Treasury yields poised for a rebound

10-year US Treasury yield, inflation expectations and real yields; difference between Asia HY and Asia IG bond yield premiums (credit spreads) and their ratio



Source: Bloomberg, Standard Chartered

	The bullish case	The bearish case
Preference order ↑	DM HY corporate ▽ ◊ ▲ + Balance sheet improvement in 2021 + Default rates to decline + Low interest rate sensitivity	– Expensive valuations – Increase in supply
	Asia USD ▽ ◊ ▲ + High average credit quality + Increasing foreign demand + Attractive valuations relative to the US	– Regulatory tightening leading to higher defaults in China – Lower yields vs other EM bonds
	EM USD government ▽ ◊ ▲ + Elevated commodity prices + Cheaper valuations vs US IG/HY bonds + EM growth rebound from late 2021	– High interest rate sensitivity – Resurgence in COVID-19 cases due to slow vaccination
	EM local currency ▽ ◆ ◊ + Elevated commodity prices + Improvement in EM FX reserves + Moderately attractive yield	– Tighter EM monetary policy – Risk of outflows due to Fed tapering – Resurgence in COVID-19 cases
	DM IG corporate ▼ ◊ ▲ + Strong credit fundamentals + Attractive hedged yield for foreign investors	– Expensive valuations – High interest rate sensitivity – Low absolute yield
	DM IG government ▼ ◊ ▲ + High credit quality + Fed, ECB unlikely to hike rates in the near future	– Improvement in growth and/or inflation – Large net issuance increase – Fed likely to begin tapering in Q1 FY22

Source: Standard Chartered Global Investment Committee

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

Equity – at a glance

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Senior Investment Strategist



Key themes

We expect global equities to continue outperforming other asset classes on a 12-month time horizon, with earnings growth expected to be the primary driver of returns. Valuations could fluctuate on concerns around Fed tapering, rising bond yields, slowing growth, regulatory tightening and COVID-19 variants. However, we expect the uptrend in global equities to remain intact. US equities remain preferred. Gradually higher bond yields could be a valuation headwind, but this is likely to be offset by still strong earnings growth. The Euro area is also preferred on expectations that the ECB will maintain its easy policy, while fund flows return to the region. The UK remains preferred. The nation's reopening strategy, if successful, could lead to a growth acceleration. In Asia, regulatory concerns continue to weigh on China, while Japan remains less preferred with its relatively weaker earnings trend.

Key chart

Earnings growth continues to drive positive equity returns, offsetting lower valuations

Fig. 13 Earnings growth is likely to be the primary driver of equity returns in H2 2021; US estimates continue to be revised higher for both 2021 and 2022

Composition of returns in global equities (left); MSCI USA's consensus EPS (right)



Source: MSCI, FactSet, Standard Chartered; *2021 returns are year-to-date

	The bullish case	The bearish case
US equities ▽ ◊ ▲	<ul style="list-style-type: none"> + Highest earnings revisions globally + Buybacks are rising + Consumers' pent up demand 	<ul style="list-style-type: none"> - Expensive valuations - Tapering of quantitative easing - Potential tax hikes
Euro area equities ▽ ◊ ▲	<ul style="list-style-type: none"> + Strong inflows from investors + Positive earnings revisions + Rotation to Value likely to resume 	<ul style="list-style-type: none"> - Spread of COVID-19 Delta variant - Fiscal stimulus lags the US
UK equities ▽ ◊ ▲	<ul style="list-style-type: none"> + Reopening; leader in vaccine rollout + Rotation to Value + Inexpensive valuations 	<ul style="list-style-type: none"> - Stronger GBP holding back gains - Monetary policy may tighten - COVID-19 hospitalisations rising
Asia ex-Japan equities ▽ ◆ △	<ul style="list-style-type: none"> + Global trade recovery + USD weakness + Undemanding valuations 	<ul style="list-style-type: none"> - Regulatory pressure in China - Geopolitical tensions - Resurgence in COVID-19
Within AXJ	South Korea equities ▲	India equities ▲ China equities ◆
Japan equities ▼ ◊ △	<ul style="list-style-type: none"> + Cyclical heavy + Global trade recovery 	<ul style="list-style-type: none"> - Weaker earnings growth trend - Resurgence in COVID-19 - Potentially stronger JPY

Source: Standard Chartered Global Investment Committee

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

FX – at a glance

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Key themes

Our 6 to 12-month outlook remains for a broadly weaker USD, as US growth radiates globally. Euro area and UK growth is likely to accelerate as high vaccination levels lead to ‘herd-immunity’ and fiscal spending is unleashed. The US twin deficits are likely to be a drag on the USD, and capital outflows seeking better risk-adjusted returns will likely boost the EUR, GBP, AUD, NZD and CAD, while the JPY and CNY remain rangebound. The key risks to our 12-month view are slower global growth, a negative shift in risk sentiment and unexpected pandemic setbacks.

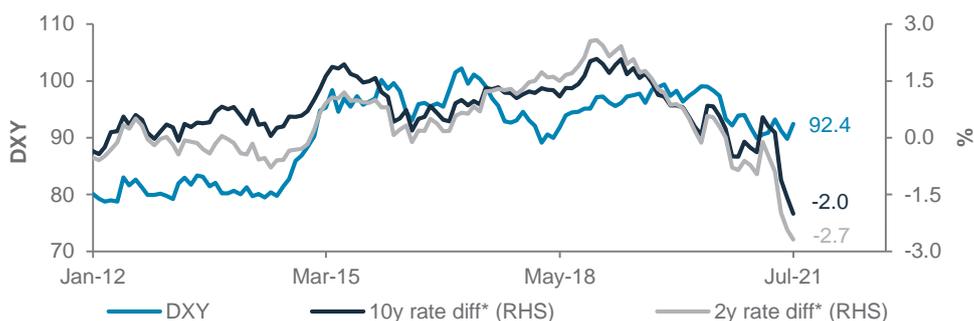
We expect a more volatile transition period over the 3-month horizon. The significant reduction in short-USD positioning suggests high levels of investor uncertainty. The outcome of the UK’s COVID-19 “vaccinate and live with it” strategy is key. Low mortality and hospitalisation rates would likely prompt other countries to follow suit, returning the focus to the positive global growth outlook and the potential for other central banks to tighten policy.

Key chart

The USD index (DXY) has responded to near-term uncertainty and short-USD positioning that has now been unwound. Once demand for the safe-haven USD ebbs as global growth rises, we expect a USD decline that reflects fundamentals, including a negative real interest rate spread

Fig. 14 Real interest rate differentials suggest an eventual USD decline

USD index (DXY), with 2y, 10y real rate differentials* between the US and peers



Source: Bloomberg, Standard Chartered; *DXY member 10y government bond yields, deflated by CPI

Fig. 15 Summary of major currency drivers

12-month outlook	The bullish case	The bearish case	12-month outlook	The bullish case	The bearish case
USD (DXY) ▼	+ US yield & growth exceptionalism + Safe-haven in a risk-off event	- Dovish Fed and ample USD supply - US twin deficits and global growth	USD/JPY ◆	+ Rising nominal US Treasury yields + Weak safe-haven demand for JPY	- Favourable real yield differentials - Short positioning; Currency hedging
EUR/USD ▲	+ Better vaccination & growth recovery + Germany vote & fiscal stimulus rise	- Pandemic wave lockdowns return - China slowdown; less fiscal stimulus	USD/CNY ◆	+ China credit impulse flat + Policy stability limits CNY gains	- Rising global trade and exports - Continued CNY investment inflows
GBP/USD ▲	+ Vaccination-led growth recovery + Bank of England has hawkish bias	- COVID-19 strategy risk - Scotland/N.Ireland post-Brexit risks	USD/CAD ▼	+ Oil, commodity price decline risk + Faster growth may be priced in	- Global/US growth positive for trade - Bank of Canada remains hawkish
AUD/USD ▲	+ Global growth and commodity prices + Stronger domestic demand	- More dovish RBA; Slow vaccinations - China demand may weaken	NZD/USD ▲	+ Hawkish RBNZ as growth rises + Terms of Trade; undervalued	- Negative global risk sentiment - Vulnerability to China demand

Source: Standard Chartered Global Investment Committee

Legend: ▲ Bullish | ▼ Bearish | ◆ Rangebound

Technicals

Manish Jaradi

Senior Investment Strategist

MSCI China: At key long-term support

The MSCI China is testing crucial support on the 200-week moving average. This follows a break below support at 102-103, suggesting that the upward pressure has faded in the interim. However, the rising slope of the long-term moving average raises the chances of a rebound from around this average, as it did in 2018. Importantly, it set the stage for a new high, as it did in early 2021. On the other hand, a lower probability scenario would be one similar to 2013-2016 – when the index fell below the 200-WMA to test the previous low (the 2013 low).

US 10-year Treasury yield: Is the uptrend over?

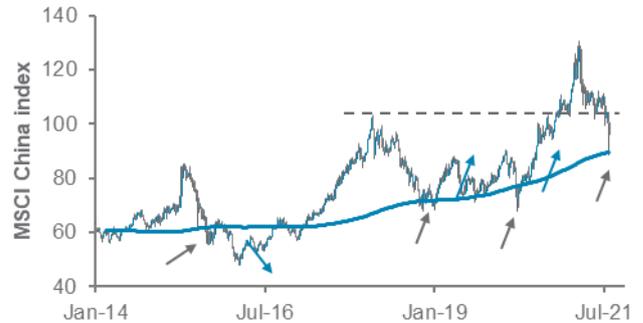
Purely based on the extent of the retreat, the move is not enough to conclude that the US 10-year Treasury yield's uptrend since last year is over. The yield has, for now, found support around the 50% retracement of the rebound from the March 2020 low, similar to 2016-2017 (the 50% retracement marked the floor). Back, then, the yield embarked on another leg higher in 2017-2018. In terms of quantum, the 2017-2018 leg higher was roughly equal to the 2016-2017 rally.

However, the pace of the recent decline is a dampener for yield bulls. It is perhaps a key differentiator vs the previous episode – a choppy drift lower (then) vs a sharp slide (now). From a psychological perspective, a choppy drift lower could signify more of position adjustments than either bulls or bears reigning supreme on a sustained basis. However, sharp declines (like now) often reflect that bears are holding an upper hand, raising the bar for another sustained leg higher.

Having said that, the yield is looking oversold, and a rebound is possible. However, for a sustained leg higher, it would need to decisively break above crucial resistance at 1.46%-1.50%. A failure to do so would imply an extended range with a retest of the mid-July low of 1.128%. Any break below 0.95%-1.00% would raise the odds of a retest of the 2020 lows. As of now, a decisive fall below 0.95%-1.00% seems like a low probability scenario.

Fig. 16 MSCI China: 200-WMA is key support

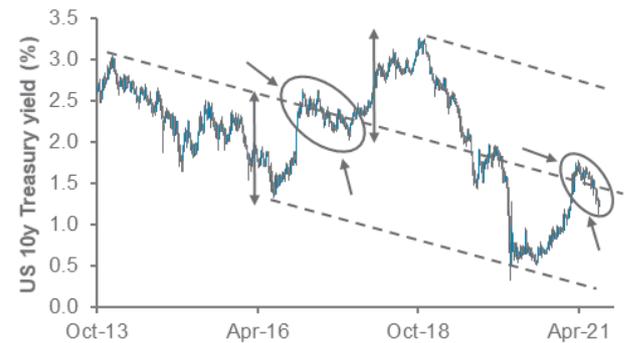
MSCI China index weekly chart with 200-WMA



Source: Bloomberg, Standard Chartered

Fig. 17 US 10-year Treasury yield: Uptrend over?

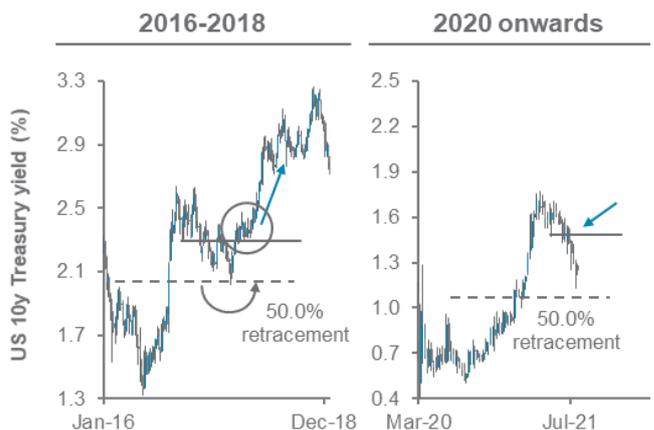
US 10y Treasury yield weekly chart



Source: Refinitiv, Standard Chartered

Fig. 18 US 10-year Treasury yield: breaking above 1.46%-1.50% is key for a sustained leg higher

US 10y Treasury yield weekly chart



Source: Refinitiv, Standard Chartered

Tracking market diversity

Francis Lim
Senior Quantitative Strategist

About our market diversity indicators

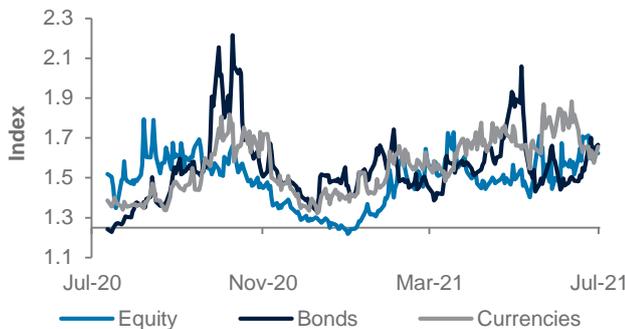
Our market diversity indicators help to identify a potential change in short-term trends due to a fall in market breadth across equities, credit, FX and commodities. When market diversity falls, it implies either buyers or sellers are dominating, leading to a rapid rise or fall in asset prices. This is usually unsustainable and is likely to be followed by a slowdown or a reversal. Our diversity indicator is based on a statistical index called fractal dimension; a value below 1.25 serves as a guideline that prices are rising or falling too fast.

Where is diversity falling or rising this month?

Market diversity across asset classes that we track remain healthy. This means the risks of a reversal to asset trends should remain contained. The recent rise in market volatility due to concerns around the COVID-19 Delta variant has, in part, helped to balance markets out of any visible crowding. For equities, this is not dissimilar to the price action we have already seen in May when the inflation fear struck and caused a temporary pullback. In any case, we have yet to see a deterrent to the longer-term uptrend in global equities, from a market diversity point of view.

Fig. 19 Average market diversity score across equities, bonds and FX

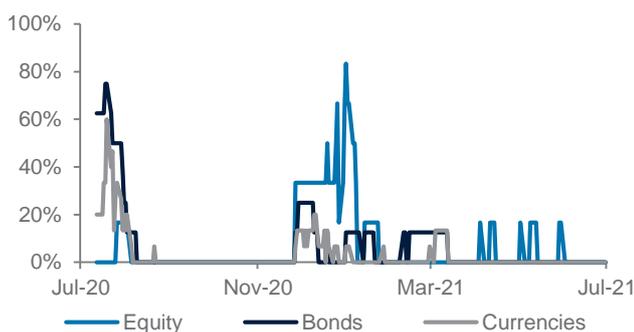
Market diversity remains healthy



Source: Standard Chartered

Fig. 20 % of assets with diversity score < 1.25

No red flags across key markets



Source: Bloomberg, Standard Chartered

For bonds, diversity has improved as their returns took a positive turn owing to lower global rates since March. Based on our diversity indicator, EM USD bonds have the lowest diversity, but even their diversity is comfortably above the 1.25 threshold.

At the sector level, weaker diversity is mostly observed in the tech and property-related sectors in China, which is not surprising as they have suffered from the recent regulatory tightening. Among these, China real estate and communication services are the two sectors with diversity currently below our threshold of 1.25. While this usually means higher odds of a reversal, we would be cautious about drawing such a conclusion in this situation given the risk regulatory tightening over-rides any diversity signal.

Fig. 21 Healthy diversity at broad asset class level, but keep an eye on sectors

Level 1	Market diversity	30-day diversity trend
FTSE World Broad IG Bond	●	↑
MSCI All Country World	●	→
Gold	●	→
HFRX Global Hedge Fund Index	●	↑
China Sectors		
Communication Services	○	↓
Real Estate	○	→
Commodities		
Natural Gas	○	↓

Source: Bloomberg, Standard Chartered; data as on 26 July 2021

Legend: ○ Very low ● Low/moderate ● High

Asset allocation summary

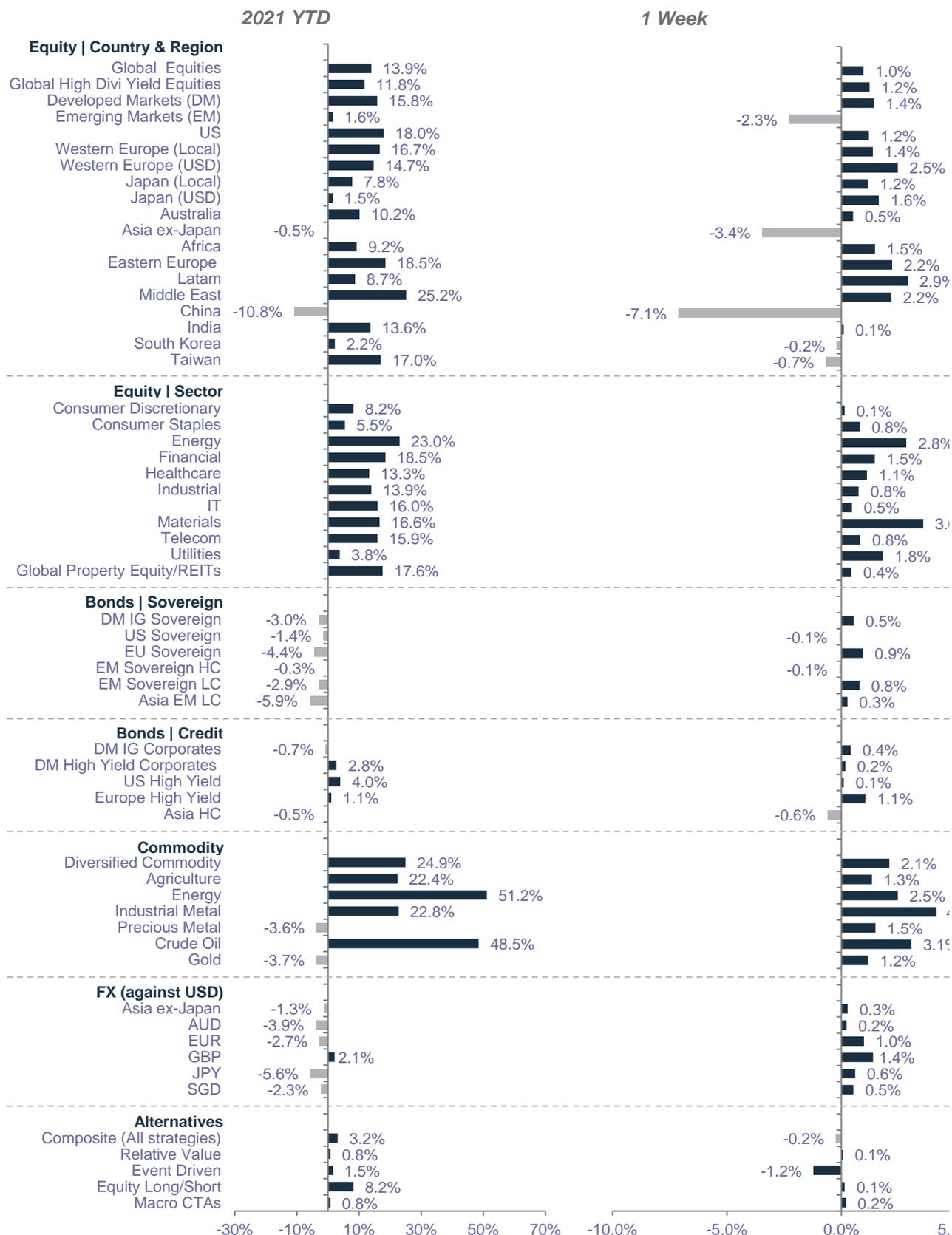
Summary	View	ASIA FOCUSED				GLOBAL FOCUSED			
		Conservative	Moderate	Moderately Aggressive	Aggressive	Conservative	Moderate	Moderately Aggressive	Aggressive
Cash	▼	12	5	2	0	12	5	2	0
Fixed Income	◆	65	39	28	7	65	39	28	7
Equity	▲	23	40	55	84	23	40	55	84
Gold	◆	0	5	5	4	0	5	5	4
Alternatives	◆	0	10	10	4	0	10	10	4
Asset class									
USD Cash	▼	12	5	2	0	12	5	2	0
DM Government Bonds	▼	4	3	2	0	6	4	3	1
DM IG Corporate Bonds	▼	6	3	2	1	8	5	4	1
DM HY Corporate Bonds	▲	12	8	5	1	18	11	8	2
EM USD Government Bonds	▲	15	9	6	2	11	7	5	1
EM Local Ccy Government Bonds	◆	11	7	5	1	8	5	4	1
Asia USD Bonds	▲	17	10	7	2	13	8	6	1
North America Equities	▲	9	15	21	32	13	23	32	50
Europe ex-UK Equities	▲	5	9	12	18	2	4	6	9
UK Equities	▲	1	2	3	4	1	2	3	4
Japan Equities	▼	0	1	1	2	0	1	1	2
Asia ex-Japan Equities	◆	5	10	14	21	4	6	9	13
Non-Asia EM Equities	◆	2	3	5	7	2	3	4	7
Gold	◆	0	5	5	4	0	5	5	4
Alternatives	◆	0	10	10	4	0	10	10	4

All figures in %. Source: Standard Chartered

Note: Allocation figures may not add up to 100 due to rounding

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

Market performance summary



Source: MSCI, JPMorgan, Citigroup, Dow Jones, HFRX, FTSE, Bloomberg, Standard Chartered

*All performance shown in USD terms, unless otherwise stated

*YTD performance data from 31 December 2020 to 29 July 2021 and 1 week-performance from 22 July 2021 to 29 July 2021

2021 key events

AUGUST 2021

05 BoE policy decision

SEPTEMBER 2021

9 ECB policy decision

22 FOMC policy decision

22 BoJ policy decision

23 BoE policy decision

26 Federal elections in Germany

OCTOBER 2021

22 Deadline for Japan General Elections

28 BoJ policy decision

28 ECB policy decision

NOVEMBER 2021

1-12 UN Climate Change Conference in Glasgow

03 FOMC policy decision

04 BoE policy decision

DECEMBER 2021

Dec China Annual Economic Work Conference

15 FOMC policy decision

16 BoE policy decision

16 ECB policy decision

17 BoJ policy decision

31 Iran's deadline for the US to end sanctions

JANUARY 2022

20 ECB policy decision

26 FOMC policy decision

FEBRUARY 2022

3 BoE policy decision

MARCH 2022

Mar China National People's Congress session

9 South Korea Presidential election

10 ECB policy decision

16 FOMC policy decision

17 BoE policy decision

27 Hong Kong Chief Executive election

APRIL 2022

Apr France Presidential elections

14 ECB policy decision

MAY 2022

4 FOMC policy decision

5 BoE policy decision

JUNE 2022

9 ECB policy decision

15 FOMC policy decision

16 BoE policy decision

■ Central bank policy | ■ Geopolitics | ■ EU politics

X – Date not confirmed | ECB – European Central Bank | FOMC – Federal Open Market Committee (US) | BoJ – Bank of Japan | BoE – Bank of England | RBA – Reserve Bank of Australia

Our key advisory publications

ANNUALLY



Annual Outlook

MONTHLY



Global Market Outlook

WEEKLY



Weekly Market View

DAILY



Global Wealth Daily

AD HOC



Market Watch



360 Perspectives



Investment Brief

Annual Outlook – The Annual Outlook highlights our key investment themes for the year, the asset classes we expect to outperform and the likely scenarios as we move through the year.

Global Market Outlook – Our monthly publication which presents the key investment themes and asset allocation views of the Global Investment Committee for the next 6-12 months.

Weekly Market View – Our weekly publication which provides an update on recent developments in global financial markets and their implications for our investment views.

Global Wealth Daily is an early morning update of major economic and political events and their day-to-day impact on various assets classes the previous day.

Market Watch focuses on major events or market developments and their likely impact on our investment views.

360 Perspectives provides a balanced assessment of the outlook for an asset class. It presents both the positives and negatives of the asset class, as well as the major drivers, instead of offering a specific view.

Investment Brief explains the rationale behind our views on an asset class, incorporating the fundamental and technical drivers.

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