WEEKLY MARKET OUTLOOK

27 April - 1 May 2015

DISCLAIMER & DISCLOSURES

Swissquote Bank SA | Ch. de la Crétaux 33, CP 319 | CH-1196 Gland | Switzerland
Tel +41 22 999 94 11 | Fax +41 22 999 94 12 | forex.analysis@swissquote.ch | www.swissquote.com/fx

WEEKLY MARKET OUTLOOK - An Overview

Economics

Weak Recovery Underway In Russia

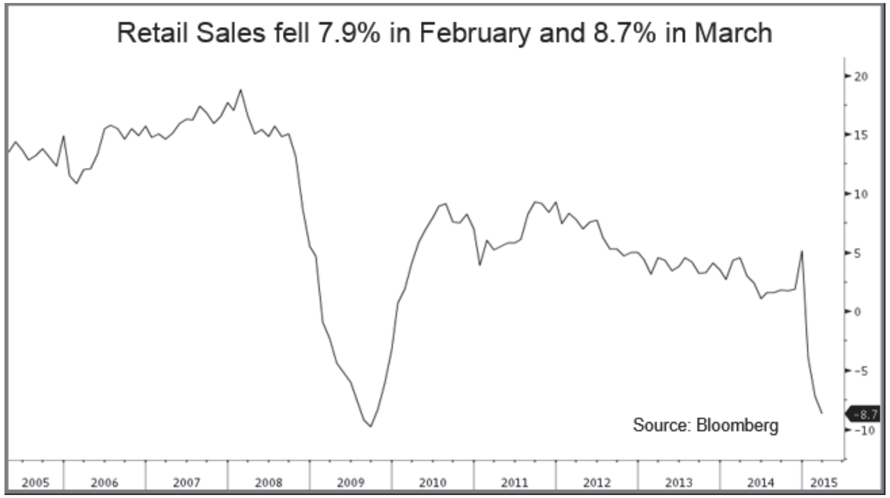
Russia's data look to have cleared the trough

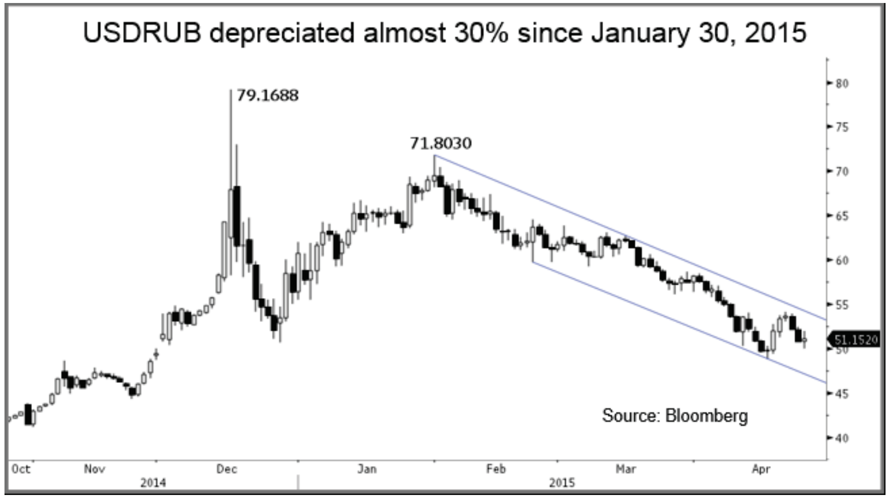
Last year, Russia was hit with a maelstrom of negative events. Oil prices were plummeting, heavily indebted corporate sector had limited access to capital markets, capital flight was putting the banking sector in jeopardy (forcing investors to question the level of Russia's massive international reserves) and western sanctions were amplifying the economic and social disorder. As a result the ruble went into a death spiral.

Yet, the all out collapse never came and Russia data look to have cleared the trough. The economic situation in Russia is stabilizing, from the collapse seen in Q4 2014. Indeed, recent economic data paint a weak but recovering picture. Consumption is an issue for growth as retail sales fell 8.7% in March following a drop of 7.2% in February. While the pace of declines have slowed, the rise in net savings suggests further contraction. The cautious consumer outlook was not helped by the unemployment rate rising from 5.3% in December to 5.8% in March, with real wages falling. However, data indicate that capital investments are improving up a solid 1.7%. Combined with good industrial production data, there is upside risk in the market, Q1 GDP forecast of -2.9%.

Stronger ruble

While actions by the central bank helped stave off the crisis, Russia's outlook remains fragile. The recession should continue as export demand and manufacturing remain weak. In addition, the stronger ruble will have a positive effect for Russia's image and inflation outlook, but is less helpful to the export outlook. Watch for USD/RUB to trend higher towards the 55 handle but upside should be limited. With energy prices improving, Russia mid-term outlook could quickly improve.





Economics

Chasing Growth

Is India the new China?

As discussed previously (see Weekly Report from last week), China's economy is growing at a slower pace, 7%y/y during the first quarter, as the second-biggest economy is facing major challenges like overcapacity of the economy, debt burden or the reorganization of its economy toward slower but sustainable growth. Investors are therefore wondering where to find some above-average long-term growth opportunities. The answer may be India. The Indian economy grew 7.5%y/y (according to the new Market-Price Calculation) during Q4 2014 while China's GDP came in at 7.3%y/y. Regarding Q1 2015, Chinese economy grew 7% while the Indian one is expected to have expanded by 7.4%.

Major challenges and monetary policy

Nevertheless, India must also deal with its own challenges to pave the way toward a solid, long-term growth. In February the government announced its intention to implement major structural reforms to put the country back on track. The package proposed by the government aimed to rationalize a capricious tax system feared by many foreign investors, to prioritize investments in infrastructure or to declare war on tax evasion. Despite these welcomed news, the government has to move from words to actions. As a good start, the government and the RBI reached a historical agreement by introducing inflation targeting monetary policy, aiming first to bring inflation below 6% by January 2016, then to set the target to 4% with a tolerance band of +/-2%.

Raghuram Rajan, the Reserve Bank of India governor, already lowered twice its policy interest rate (repo rate) by 25bps down to 7.5% during two unscheduled meetings (February and March). The governor is taking advantage of low inflationary pressure (5.11%y/y in January, 5.19% in February and 5.17% in March) and still has room to lower rates further. Mr. Rajan didn't cut rate on April 7, waiting on banks to transmit those rates cuts to the real economy as the base rate is still at 10%y/y. However, India has to take into account monetary policy of other countries as currency war rages across the globe. The Fed will certainly postpone the first rate hike later this year, we expect the RBA to cut rates in May while China just cut its RRR to 18.5% and is ready to ease further its monetary policy. We believe that the RBI is prone to cut rates as it wrote in its First Bi-monthly Monetary Policy Statement (released on April 7): 'Going forward, the accommodative stance of monetary policy will be maintained, but monetary policy action will be conditioned by incoming data'.

We therefore think that the RBI still has room to act and we expect the central bank to lower its repo rate by at least 25bps to 7.25% in its next policy meeting on June 2. However, the RBI may trigger a rate cut during an unscheduled meeting if inflation remains subdued.

FX Markets

SNB Tightened Exemption Rules

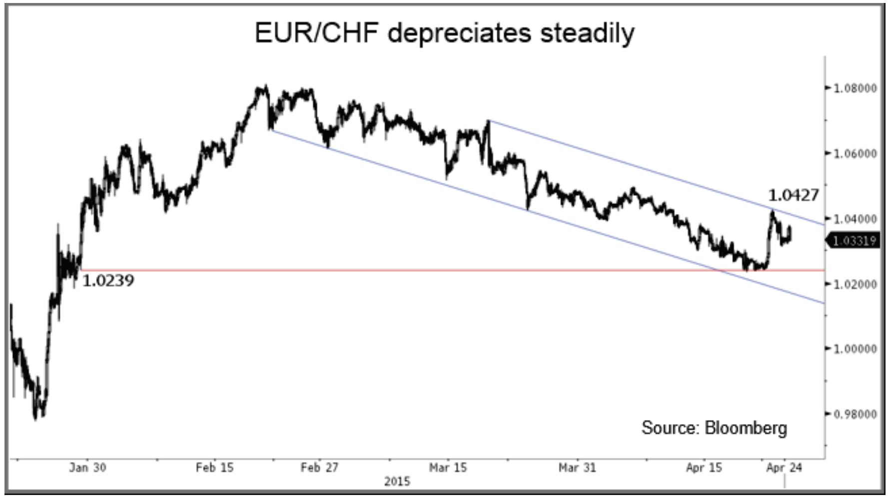
New rules

After a few months of uncertainty during which investors tried to determine whether the SNB was actively defending the implicit target of 1.05-1.10 band in EUR/CHF, traders have begun to challenge the SNB by pushing the Swiss franc slowly but surely towards parity. Since February 20, EUR/CHF lost more than 5%, from 1.0811 to 1.0236 on April 21. The market quickly realised that the 1.05-1.10 band was more a trading floor rumour than a reality. On April 22, the SNB surprised the market by announcing stricter exemption rules as institutions associated with the Confederation, such as the pension fund of the Confederation or the pension fund of the SNB, are no longer exempt of negative interest. Consequently, only the account holders of the national social security system (AVS/IV/EO, IV/AI and EO/APG) are still fully exempt. However, this decision doesn't change the rule for domestic banks as the "20 times minimum reserve requirement" still holds. Total sight deposits of domestic banks at the SNB increased by CHF1.4bn to around CHF380bn over the previous week while 20x the minimum requirement corresponds to CHF290bn.

What is next?

The SNB is running out of solution and is struggling to stop the appreciation of the Swiss franc as the ECB buys EUR60bn worth of sovereign bonds every month, in an attempt to boost Eurozone's economy, dragging the euro lower. The most powerful tool left is the exemption threshold; so far it is set to 20 times the minimum reserve requirement but the Bank could lower this threshold to increase the sight deposits exposed to negative rates. This move would force domestic banks to transfer these costs to retail deposits or to start chasing higher returns abroad. Other solutions would be to lower interest rates further into negative territory or to intervene in the foreign exchange market. We believe that the last two solutions are unlikely as the recent monetary actions suggest that the SNB is reluctant to increase massively its balance sheet. A solution may come from the Eurozone. In case of Greece and the Eurozone finally reach an agreement, foreign investors may stop avoiding European assets.

All in all, we don't think that the decision made on April 22 will fundamentally change the EUR/CHF situation, especially as the resulting policy has marginally changed. The main goal was to remind traders that the SNB is not pleased by the current valuation of the Swiss franc. The focus, therefore, remains on the development of the Greek situation and the ECB's bonds buying program. We expect the EUR/CHF to erase previous gains and decline towards parity.



FX Markets

The RBA Unlikely To Lower Rates Below 2%

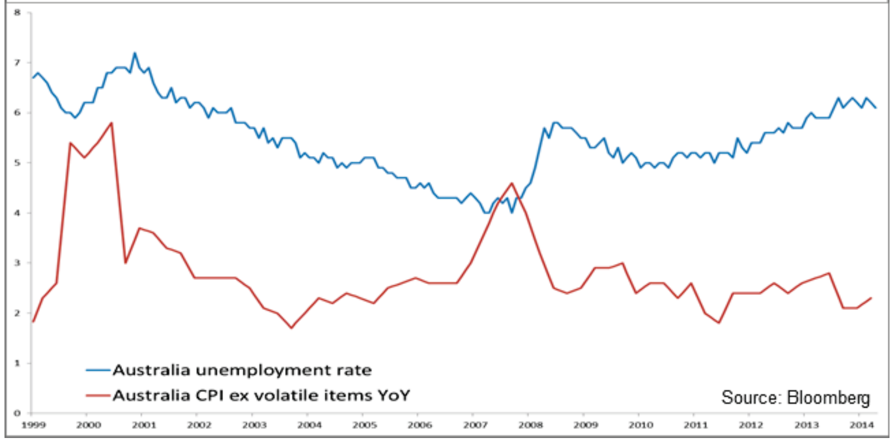
Recent data has weakened our call for a rate cut in May

The recent strong employment and inflation data in Australia have weakened our call for a rate cut in May. Indeed, March labour data were better than expected and may challenge the pessimistic view of the Australian central bank. Furthermore, March inflation, although weak at the headline level, slightly increases at the core level and remains above the 2% threshold with a strong participation among segments. Coupled with the publication of the April RBA board minutes, which continues to highlight a high degree of concern about the housing market, the odds that the Reserve Bank of Australia stays on the sidelines have increased. However, we still favour a rate cut in May. Indeed, the ongoing decline in the Australian terms of trade, the soft growth outlook and a weaker growth in China should tilt the balance towards a rate cut.

What does it mean for AUD/USD?

One of the key driver in the decline of AUD/USD has been the willingness of the RBA to favour a lower domestic currency. However, with Sydney housing prices seen as "rather exuberant" by governor Stevens and underlying inflation comfortably moving in the 2-3% RBA's target range, the cost of easing has significantly increased. In that respect, a further rate cut below 2% seems now very remote. As a result, the pace of the US tightening cycle will be more influential, suggesting a reduced drag for AUD/USD in the next months. Looking at the price behaviour, the recent stabilisation in place since February confirms a less impulsive decline. Consequently, while we continue to favour a bearish bias on AUD/USD, we suspect that entry points have to be revised higher, where prices are more overbought and/or closer to key resistance levels. Currently, prices close to the resistance at 0.7938 (24/03/2015 high) is our best guess especially given the other key resistance at 0.8025 (28/01/2015). A break of the strong resistance at 0.8295 (15/01/2015 high) is needed to suggest a change in the underlying declining trend in AUD/USD.

Unemployment has not worsened and core CPI stays above 2%



Source: Bloomberg

Sell on strength remains our preferred strategy on AUD/USD

Source: Swissquote, Bloomberg

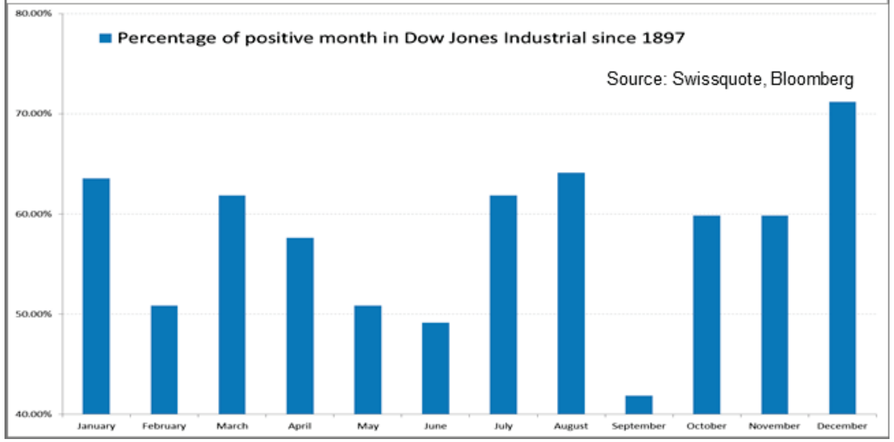
Stock Markets

Sell In May And Go Away

Seasonality is now less supportive for US equities

A rather well-known adage in the stock market is "sell in May and go away". It is based on the idea to hold US equities at the beginning of November and to liquidate them at the end of April. It does not mean that the stock market will decline from 1 May to the end of October, only that the performance during that time has been found empirically lower than the rest of the year. Although part of the difference in performance comes from a reoccurrence of major market declines near September (e.g. 1987, 1998 and 2008), it shouldn't overshadow some recurrent facts. The month of September is by far the worst month to hold US equities, as it is positive roughly only four times out of ten (41.88%). The only other month to be on average more often negative than positive is June but only by a small margin (49.15%). On the other hand, the month of December is by far the best month to hold US equities, as it is positive more than 7 times out of ten (71.19%).

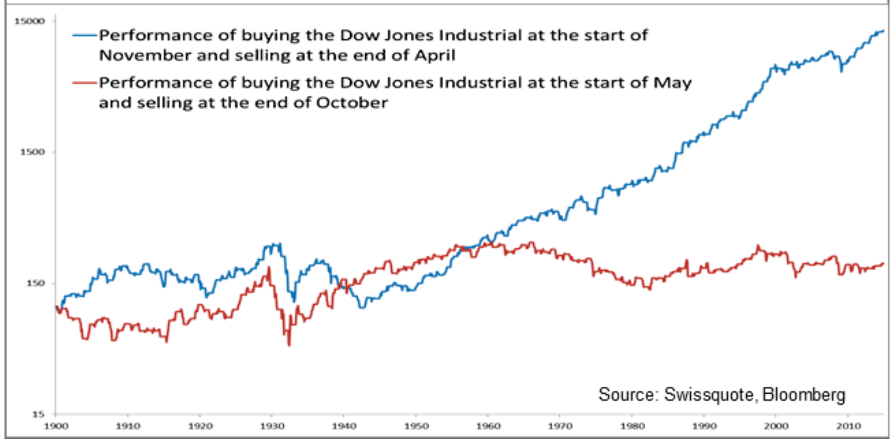
September is by far the worst month to hold US equities



What does it mean for 2015?

Although the S&P 500 has not been able to make significant new highs since February yet, the upcoming less supportive seasonality does not call for a major decline in the near-term. Part of the reasons are that the recent rally in US equities is broad-based (mid and small caps are confirming the strength in the large cap) and that the current technical configuration (ascending triangle) favours a short-term bullish bias. However, with the Fed looking to start its tightening cycle this year (probably in September), we suspect that the trading period around September is likely to be rather volatile. As a result, we would not be surprised to see some profit taking in the next months as we approach the end of the summer, confirming subdued returns for the period of time from May to October.

Since 1950, seasonality has added significant outperformance



FX Markets

Net Short JPY Positioning Is In Neutral Territory

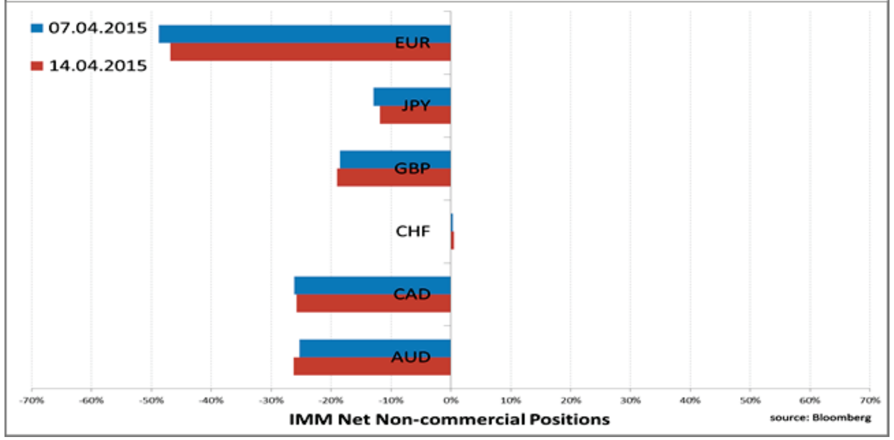
The International Monetary Market (IMM) non-commercial positioning is used to visualise the flow of funds from one currency to another. It is usually viewed as a contrarian indicator when it reaches an extreme in positioning.

The IMM data covers investors' positions for the week ending 14 April 2015.

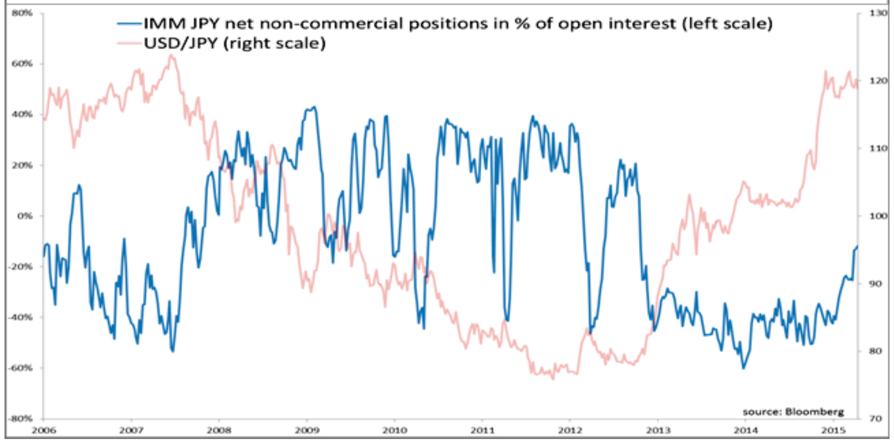
Changes in FX positioning were very limited. Despite the reduction in net short EUR positions, the current levels remain in stretched territory. As a result, positioning continues to act as an obstacle for further short-term weakness in the EUR/USD. Net short JPY positions also saw a small decrease. Although we suspect that the Bank of Japan is unlikely to unveil any bold new expansionary measures, the current neutral positioning, the weak Japanese inflation outlook and the upcoming Fed's tightening cycle make a long USD/JPY position quite attractive in the second half of the year.

Net short CAD positions are expected to be further reduced as the Bank of Canada is getting increasingly likely with its current monetary policy and may even start to consider raising rates. As a result, further weakness in CAD is expected.

No change in FX positioning



Net JPY positioning is in neutral territory



DISCLAIMER

While every effort has been made to ensure that the data quoted and used for the research behind this document is reliable, there is no guarantee that it is correct, and Swissquote Bank and its subsidiaries can accept no liability whatsoever in respect of any errors or omissions, or regarding the accuracy, completeness or reliability of the information contained herein. This document does not constitute a recommendation to sell and/or buy any financial products and is not to be considered as a solicitation and/or an offer to enter into any transaction. This document is a piece of economic research and is not intended to constitute investment advice, nor to solicit dealing in securities or in any other kind of investments.

Although every investment involves some degree of risk, the risk of loss trading off-exchange forex contracts can be substantial. Therefore if you are considering trading in this market, you should be aware of the risks associated with this product so you can make an informed decision prior to investing. The material presented here is not to be construed as trading advice or strategy. Swissquote Bank makes a strong effort to use reliable, expansive information, but we make no representation that it is accurate or complete. In addition, we have no obligation to notify you when opinions or data in this material change. Any prices stated in this report are for information purposes only and do not represent valuations for individual securities or other instruments.

This report is for distribution only under such circumstances as may be permitted by applicable law. Nothing in this report constitutes a representation that any investment strategy or recommendation contained herein is suitable or appropriate to a recipient's individual circumstances or otherwise constitutes a personal recommendation. It is published solely for information purposes, it does not constitute an advertisement and is not to be construed as a solicitation or an offer to buy or sell any securities or related financial instruments in any jurisdiction. No representation or warranty, either express or implied, is provided in relation to the accuracy, completeness or reliability of the information contained herein, except with respect to information concerning Swissquote Bank, its subsidiaries and affiliates, nor is it intended to be a complete statement or summary of the securities, markets or developments referred to in the report. Swissquote Bank does not undertake that investors will obtain profits, nor will it share with investors any investment profits nor accept any liability for any investment losses. Investments involve risks and investors should exercise prudence in making their investment decisions. The report should not be regarded by recipients as a substitute for the exercise of their own judgment. Any opinions expressed in this report are for information purpose only and are subject to change without notice and may differ or be contrary to opinions expressed by other business areas or groups of Swissquote Bank as a result of using different assumptions and criteria. Swissquote Bank shall not be bound or liable for any transaction, result, gain or loss, based on this report, in whole or in part.

Research will initiate, update and cease coverage solely at the discretion of Swissquote Bank Strategy Desk. The analysis contained herein is based on numerous assumptions. Different assumptions could result in materially different results. The analyst(s) responsible for the preparation of this report may interact with trading desk personnel, sales personnel and other constituencies for the purpose of gathering, synthesizing and interpreting market information. Swissquote Bank is under no obligation to update or keep current the information contained herein and not liable for any result, gain or loss, based on this information, in whole or in part.

Swissquote Bank specifically prohibits the redistribution of this material in whole or in part without the written permission of Swissquote Bank and Swissquote Bank accepts no liability whatsoever for the actions of third parties in this respect.