WEEKLY MARKET OUTLOOK

6 - 12 July 2015

DISCLAIMER & DISCLOSURES

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WEEKLY MARKET OUTLOOK - An Overview

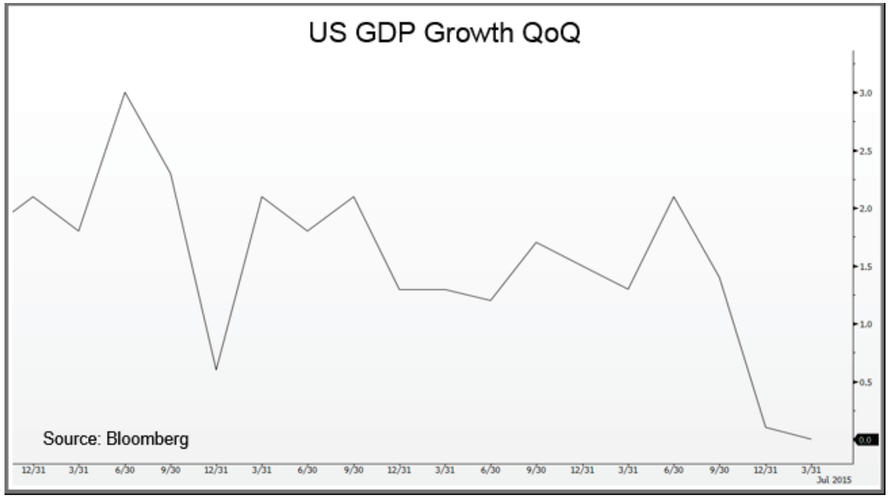
Economics

Speculations On A September Fed Rate Hike Moves Away

Non-farm payrolls came in last week lower than expectations at 223K. Unemployment rate printed at 5.3% vs 5.5% a month earlier. Those data are well considered by markets and an adverse outcome is diminishing expectations about a September rate hike. Last Tuesday's ADP Jobs reports came in largely over expectations with 237K new private jobs added vs 218K expected. This data missed to be a good indicator of US non-farm payroll.

For the time being, even if the traders are focused on the Greek referendum, markets is considering closely those data in order to assess the likelihood of a rate hike in September. Over the last few months, US data came in mixed, both strong (unemployment rate) and disappointing (home sales, consumer expectations, NFP). The pressure is still on the job market as a rate hike in September is highly dependent of a sound labour market. Furthermore, the NFP report missed to keep on fuelling a virtuous circle. A more dynamic job market would increase consumer confidence and consumer spending which would be necessary to reach the 2% inflation target. The Fed wants also to feel more confident about the ability to achieve this target before increasing rates. This is why we think that US data are still insufficient for markets to correctly price a September rate hike. We need an additional inflation pressure. June CPI will be released in a couple of weeks. It will provide reasonable grounds that the 2% target is reachable. Without those basics, the Fed will take a huge risk increasing the rate. Aside inflation figures, Q2 GDP will give the final point of rate hike speculations for September and markets will start considering 2016 as a decent outcome.

EURUSD price action is driven by Greece's referendum, however against a backdrop of US recovery, the pair should gain downside momentum. As long as there are serious talks of increasing rates, the greenback will strengthen.



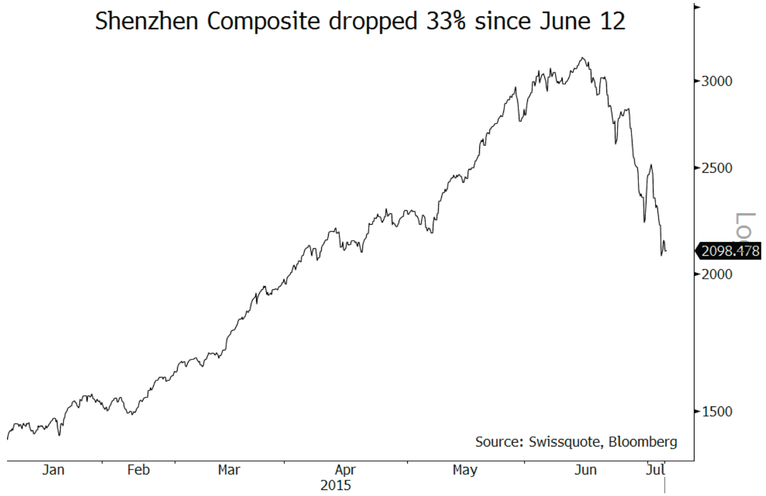
Economics

Chinese Shares Suffer Worst Sell-Off Since 2008

On June 12, the Shanghai Composite was up more than 60% since the beginning of the year while its tech-heavy counterpart, the Shenzhen Composite, gained 123% over the same period. While stock markets were printing new records every day as the People's Bank of China eased its monetary policy further, we saw and we are still seeing no improvement in the Chinese economy.

Latest data from China show that there is still no sign of rebound as June HSBC Composite contracted for the third straight month to 50.6 while Services PMI dropped to 51.8 from 53.5 in May. A couple of days earlier, HSBC Manufacturing PMI dropped to 49.4 and confirmed that the manufacturing sector is shrinking. The PBoC is now in easing mode for almost a year and is still struggling to cushion the slowdown of the world's second biggest economy. Last weekend, the Bank reduced both the 1-year lending rate by 25bps to 4.85% and the reserve requirement ratio for certain banks. We expect the PBoC to ease further its monetary policy in the coming months.

As expected, Chinese stock markets benefited most from the PBoC monetary policy and rallied to record highs with the Shenzhen Composite printing at all-time highs, forcing China's securities regulator to tighten rules on margin lending earlier in May to try to limit the risks from any market bust. Nevertheless, what was bound to happen has happened and stock markets entered into correction mode (still not sure if the bubble had burst) as investors dumped stocks to meet margin calls, accelerating the sell-off. As a result, China Securities Regulatory Commission try to buoy the market last Thursday by loosening rules on margin financing. It didn't work. Chinese stock markets are now officially in bear market and we do not recommend to buy on dip as the sell-off is certainly not over. Late on Thursday, the CSRC opened an investigation into market manipulation as it suspect that hundreds of companies suspended trading of their shares in order to avoid their stock price to drop further. The CSRC is also trying to prevent short-selling by discouraging traders to speculate on the fall of the stock market. Nonetheless, the CSRC needs to understand that the purpose of futures is for risk management and remain the primary tool used by hedgers, meaning that short-selling is actually essential. It seems that China's regulators are trying to control the stock market in the same way the renminbi is controlled and that they only want the economic benefit of a free stock exchange and not the shortcomings.



Economics

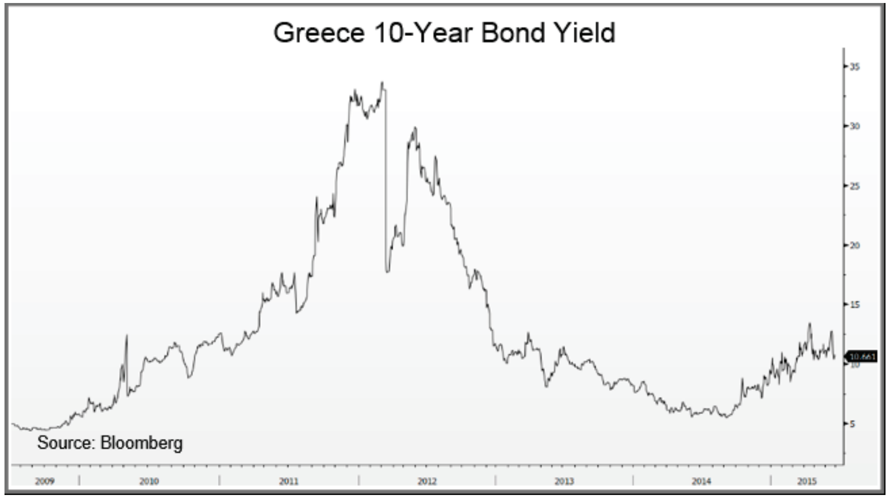
Greece In The Eye Of The Storm

Negotiations have been tensed last weekend between Greece and Eurogroup members. Intensity reached a climax when, against all odds, Alexis Tsipras announced last Saturday night that a referendum will take place on July 5th. People will be asked to agree with creditors' proposal. Greek Government, which failed to reach a deal with its creditors, is certainly trying to get the support from its people in the likely case that Greece will exit the Eurozone.

Greece missed the €1.6 billion payment to the IMF last Tuesday. Mounting uncertainties Greece's EU membership have boosted bank withdrawals. Over the last two years, €30 million were going out the Greek system in average during weekends. It has been more than € 1 billion that have been withdrawn this weekend. Last week, ECB announced that the Emergency Liquidity Assistance (ELA) was renewed on same levels. But already most of the liquidities provided have been withdrawn. Therefore, Greek government has been compelled to install drastic capital controls (€60 per person and per day). Furthermore, until the referendum takes place, Greek banks and Athens Stock Exchange are shut down. However it is worth adding that in case of a very unlikely agreement with Brussels, the referendum will be cancelled.

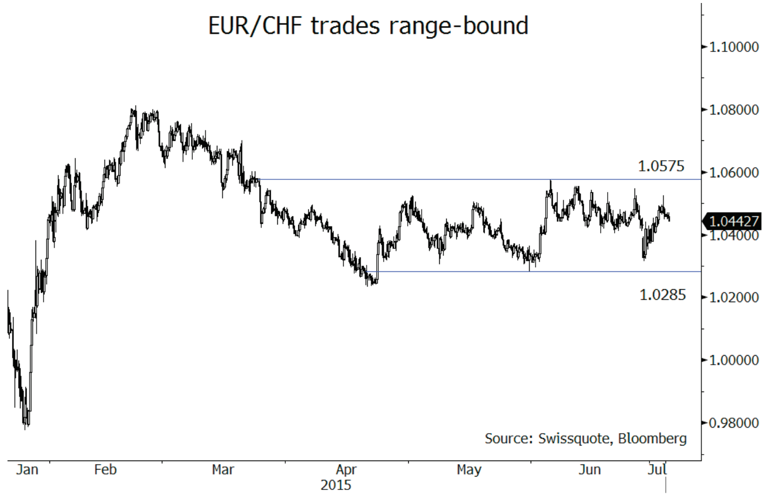
Another key issue concerns Credit Default Swaps. In case of a Greek default, will CDS' payments be triggered? European banks' exposure is huge and rating agencies stated did not lower Greek grade to D (default) after the default payment to the IMF. It has been said that a failure to reimburse the aid bailout does not constitute a proper default. We now wonder what will happen when Greece will fail to reimburse its core debt at the ECB next payment on July 20th. From those uncertainties, we are clearly bearish on European Bank stocks.

Markets is now turning to risk-off, moving out from Stocks to Bonds. German 10-year yield is trading around 0.817%. In addition, investors are getting rid of peripheral bonds, pushing Italian and Spanish yields higher. Fear that a contagion will happen is growing.



Economics

Switzerland's Economy Struggles



Swiss KOF indicator reached 3-year low

After a slight uptick in May, KOF leading indicator dropped to 89.66 in June, its lowest level since December 2011. In addition, June manufacturing PMI surprised to the upside with a reading of 50 versus 49.9 expected and 49.4 in May. The index just reached the 50% threshold, indicating that the industry adapted, to some extent, to a lower EUR/CHF. The index was driven higher by production output (rose from 51.7 to 54.8), stocks of finished goods (50.1 versus 47.1 in May) and purchased prices (43.2 from 40.9 previous reading). However, the picture is not that bright as the backlog of orders contracted from 51.4 to 51.1 while the quantity of purchase dropped to 50.3 from 52.5.

The highly resilient Swiss economy is clearly feeling the consequences of a strong Swiss franc and the economic outlook does not look great. In addition, the Greek situation is also weighing on the Swiss franc as investors shun risk and flee to safe-havens. Last Tuesday in Bern, the SNB declared that it had intervene in the currency market on Sunday night to stabilise the Swiss franc amid Greek deadlock. Thomas Jordan refused to give details about the scale of the intervention but we believe it wasn't a massive intervention as the SNB has remained moderately active in the FX market lately. Indeed, sight deposits increased by a weekly average of CHF634mn during the month of June, compared to CHF1,368mn in May and CHF882mn in April. Despite the SNB's willingness to reduce traders' interest for Swiss franc by intervening in the foreign exchange market, the CHF will remain in demand as long as the long-term situation do not improve substantially in euro zone economy together with a long-term resolution of the Greek crisis. We expect EUR/CHF to trade sideways and to remain within the 1.0250-1.05 range. However, be ready to see some big swings Monday morning !

FX Markets | IMM Non-Commercial Positioning

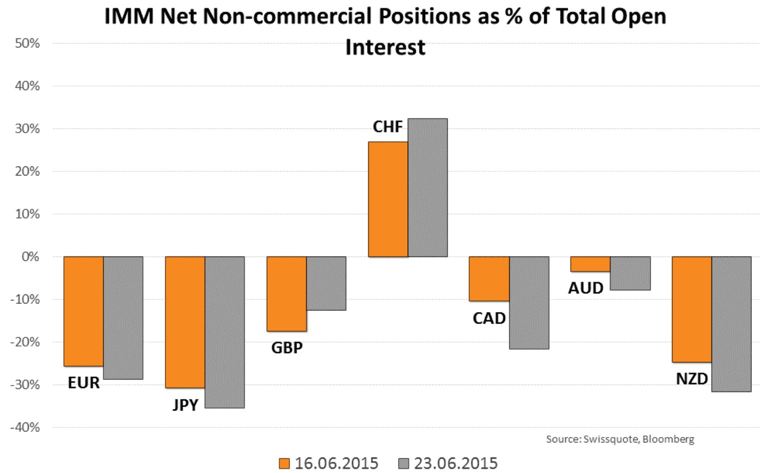
The International Monetary Market (IMM) non-commercial positioning is used to visualise the flow of funds from one currency to another. It is usually viewed as a contrarian indicator when it reaches an extreme in positioning.

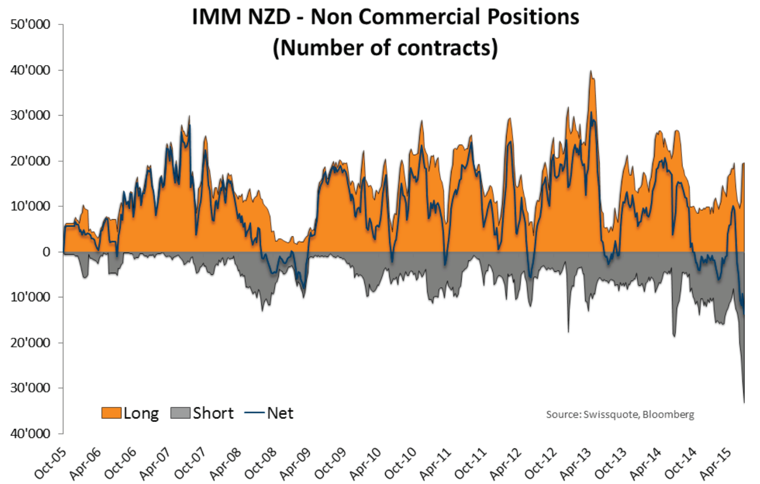
The IMM data covers investors' positions for the week ending 23 June 2015.

The NZD net short positions have increased considerably since April 2015 and are expected to increase further as the Reserve Bank of New Zealand made crystal clear that New Zealand's economy needs further NZD depreciation in order to counterbalance declining commodity prices.

All currencies have seen an increase in their net short positions with the exception of the pound sterling and the Swiss franc.

Net short positions in EUR and JPY are already elevated. As a result, we suspect a limited downside potential in the next few weeks.





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