WEEKLY MARKET OUTLOOK

9 - 15 November 2015

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

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WEEKLY MARKET OUTLOOK - An Overview

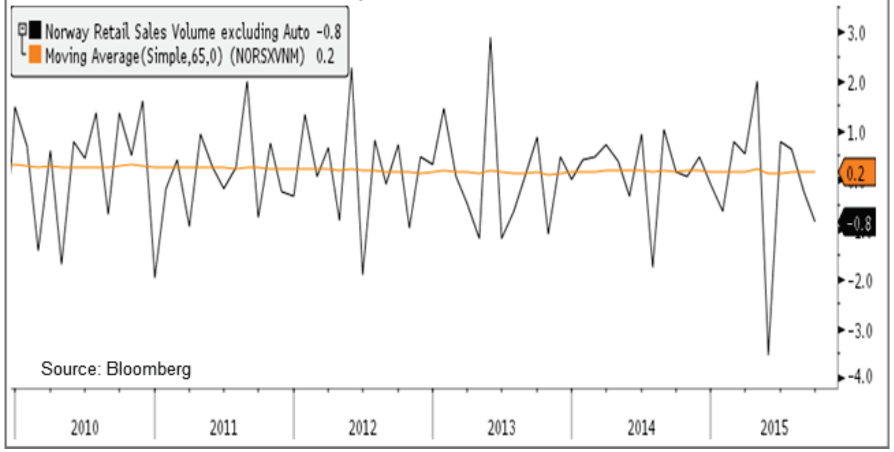
Economics

Norges Bank To Cut Rates

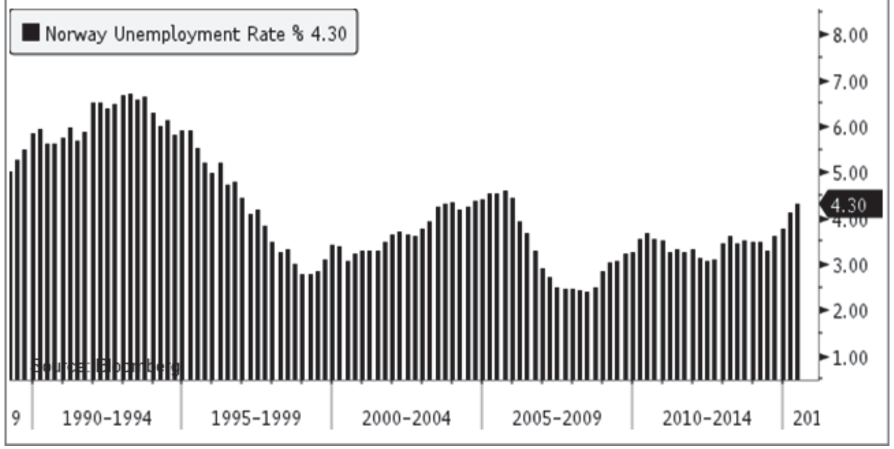
While the BoE grabbed the spot light last week, the Norges Banks also provided further indications that a primary theme for 2016 will be dovish central banks. As was widely expected, the Norges Bank held key policy rates at 0.75%. The overall assessment was slightly more neutral than September, but only by a hair. The bank noted that the economy had weakened more than expected since the September meeting. The bank pointed to declining household consumption as a primary culprit. In regards to inflation, it was broadly in-line with expectations although the weaker NOK would equate to disinflation pressure. The accompanying statement reiterated September's easing bias but did not provide any clear signals that the bank would ease rates in 2015. Governor Olsen provided a balanced outlook, noting that since September "some factors" support raising rates and "some factors" support cutting rates. However, with the economic data and outlook showing concerning decelerations, we anticipate a 25bp cut at the December meeting.

Norway's industrial production in September increased by 1.6% m/m against 1.7% prior read. The year-on-year growth rate slowed to 2.0% from 3.1%. While the industrial sector has held up relatively well there is a clear flat lining of momentum suggesting that GDP growth will also decline. Retail sales 3Q released in October fell -0.8% following a decline of -0.4% indicating that the consumer is suffering as the effect of lower oil prices persist. In addition, with unemployment rates rising to 4.6% from 4.3%, there is the risk that a deeper consumption driven slowing will take hold. The Norges Bank will cut rates in December to halt the growing decay in confidence spreading through Norway. With the market pricing roughly only 10bp of easing in December, a cut will catch the market flat footed. We remain negative on the NOK and forecast the EURNOK should head back to year highs around 9.61.

Consumption driven slowdown



Weakness due to low oil prices



Economics

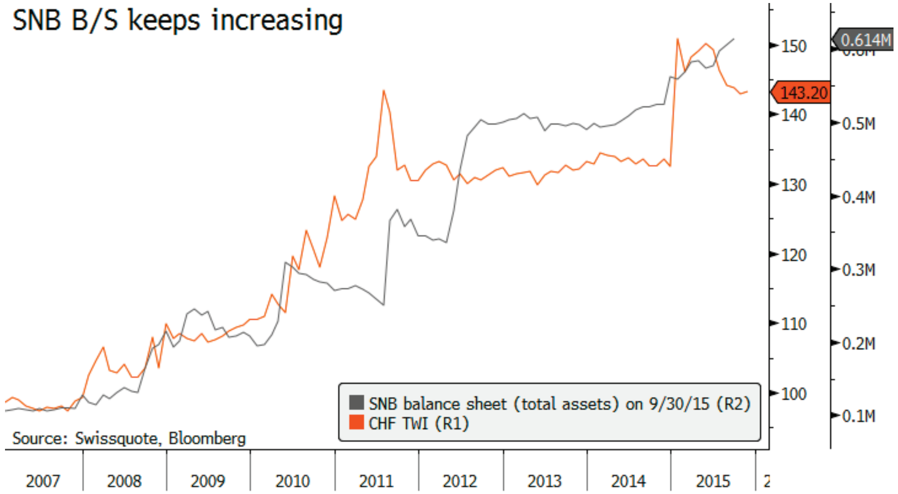
ECB Has Cornered The Swiss National Bank

CPI surpises to the upside

In October, CPI contracted 1.4% on a year-over-year basis, as the effect of the peg removal endures. On a month-over-month basis, inflation level rose 0.1%, beating market expectations of a flat reading. This improvement came against the backdrop of a weaker Swiss franc which is making foreign goods more expensive for Swiss people - the price of foreign goods increased by 0.8%m/m. When looking at the core gauge, inflation rose 0.2%m/m, while on a year-over-year basis prices contracted 0.8%.

Limited option for the SNB

In spite of this slight improvement, we do not believe the underlying story has changed as the strong Swiss franc continues to weigh on the Swiss economic and inflationary outlook and it is about to get worse. The ECB's stated intention to support further the EU economy is certainly keeping SNB's officials awake at night especially given the limited number of weapons in their arsenal. What are the possible ways in which the SNB can react? Let's do a quick review. We can almost certainly rule out a potentially massive FX intervention as the central bank's balance is already at stratospheric levels. Secondly, we don't believe it's likely that there will be a tightening of the exemption rule since it would directly impact the saving accounts of Swiss people. So what could happen? From our standpoint, the SNB will most likely respond by pushing rates further into negative territory and we believe that Mr. Jordan could combine such a measure with a raise of the exemption threshold. On the medium-term EUR/CHF remains in its declining channel, while on the short-term we do not rule out a temporary appreciation of the euro.

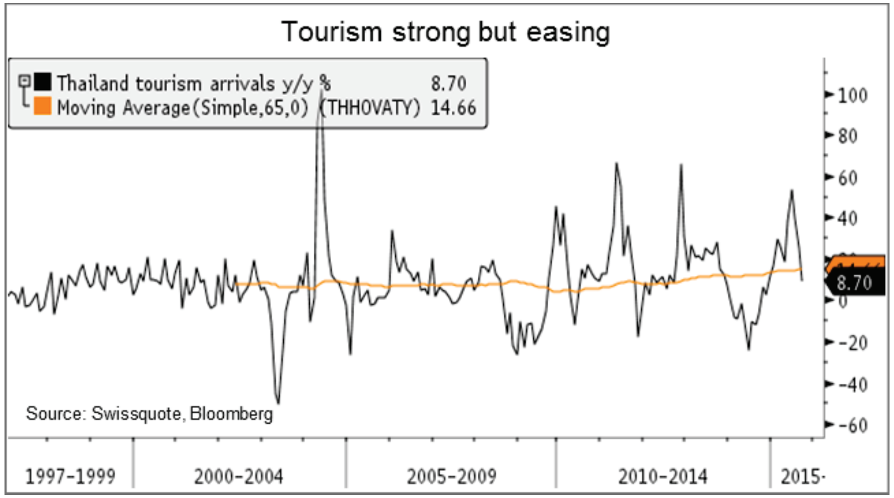


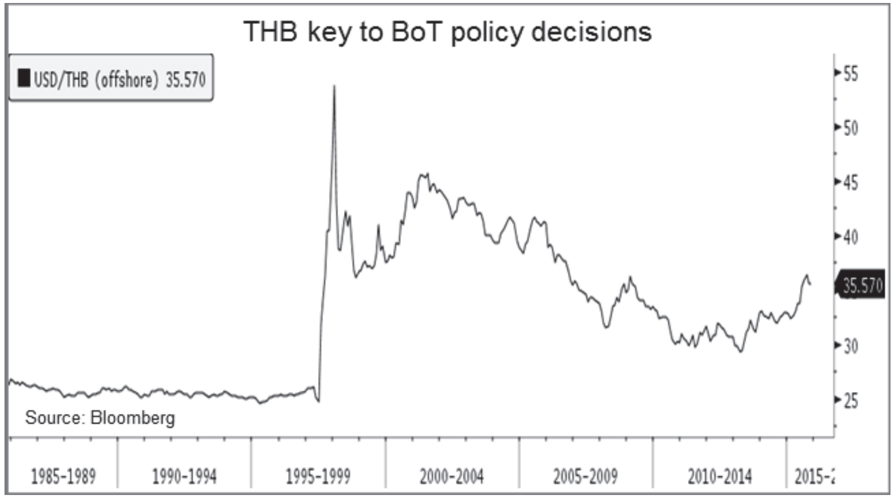
Economics

BoT Sidelined For Now

As we had expected the Bank of Thailand held its policy interest rate unchanged at 1.50%. The unanimous vote against change clearly signified that the MPC members do not see any critical threats to Thailand's economy, choosing rather to keep their `powder dry` just in case downside pressures intensify. The guidance provided within the statement remains dovish. The statement reiterated that that government stimulus spending was critical in supporting the economy. Growth is currently tracking expectations but continues to be effected by external slowing global growth and financial market volatility. Domestically, tourism and fiscal support were the main drivers for business activity. Thailand has seen a worrying decrease in exports by 5.51% and industrial output fell 3.36%, while CPI for October came in at -0.77% y/y, in negative territory for the 10th straight month. However, there is mounting evidence that the economy has bottomed and should be improving moving forward.

Despite the softness in recent economic data, we suspect that the BoT will view monetary conditions sufficiently accommodative. New BoT governor Veerathai Santiprabob indicated that the environment will remain challenging for the next 2-3 years. However, policy must balance support for economic growth with risks of financial instability which come with low rates for an extended period. The primary disruption to our expectations for the BoT to remain on the sidelines would be the appreciation of the THB versus its regional peers. Baring the ability to verbally manage the exchange rates, the BoT will be forced to cut rates to halt growth disrupting baht strength.





Economics

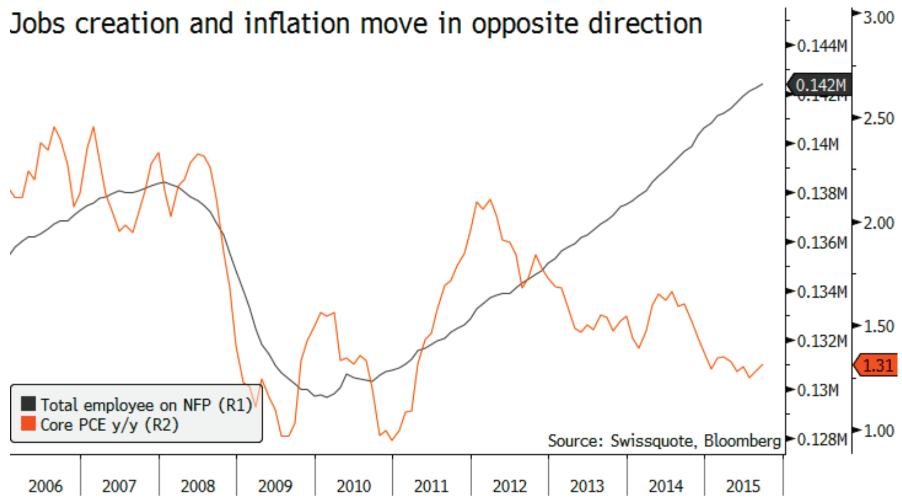
US: Inflation Reports Will Be Key

The last job report was a massive surprise. NFPs printed at 271k versus 185k expected. Market participants are now confident that Yellen will start raising rates in December. However, we prefer to be cautiously optimistic as the four previous NFP reports disappointed massively to the downside. It is therefore more a "catching up" than a clear lift-off signal. The next job report (the last one before the December FOMC meeting) will be crucial as it will confirm Friday's results.

However, from our standpoint, the market is overestimating the importance of NFPs when trying to anticipate any monetary policy decision as it is always subject to important revision. Moreover, the job market has improved persistently over the last few months, but the Fed has remained side-lined. We believe that inflation levels and the global economic outlook - especially when it impacts directly the US - are of greater influence when trying to predict Yellen's next move. So where do we stand? The Fed's favourite inflation gauge, the Core PCE deflator, remained stable at 1.3%y/y in September, below median forecast of 1.4%. When looking at the indicator including the most volatile prices - such as energy and food prices - the picture does look even uglier as prices rose by only 0.2%y/y.

Finally, when we have a look at the "external factors" or the so-called Fed's third mandate, it is also not supportive of a rate hike in December. First of all, most central banks across the globe are currently easing and are even thinking about increasing the size of their stimulus. The Riksbank increased the size of its QE last week, while the ECB made clear that an extension/increase of its bond purchase programme is just a matter of time. Moreover, even if the BoJ continues to present an optimistic view of its economy, the central bank has consistently missed its targets… The Fed is therefore alone against the world. Furthermore, let's imagine Yellen finally decides to lift rates for some reasons. Higher interest rates in the US mean a stronger dollar, which means lower inflation. And the Fed does not want to have to deal with disinflationary threats.

Nevertheless, what made a big difference last Friday is the clear improvement in wage growth. Average hourly earnings increased 2.5%y/y, beating market expectation of 2.3%. Therefore, if inflation starts to clearly pick up, it would be a game changer. The upcoming inflation reports will be key for the timing of lift-off.



FX Markets

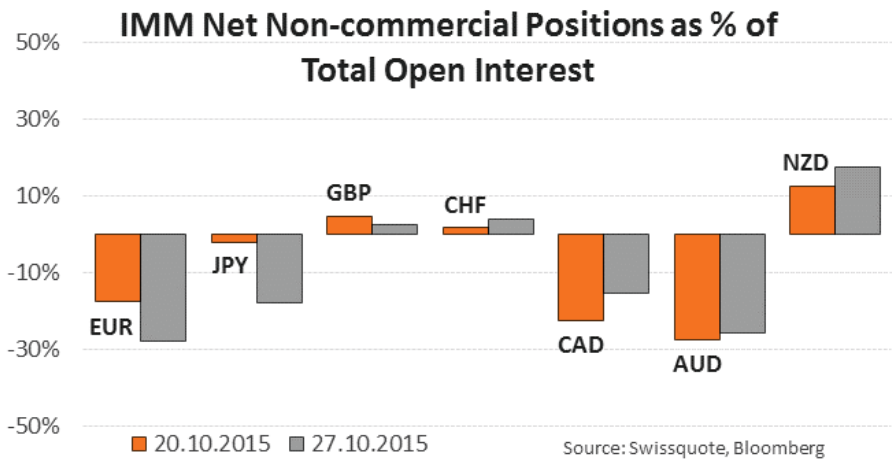
IMM Non-Commercial Positioning

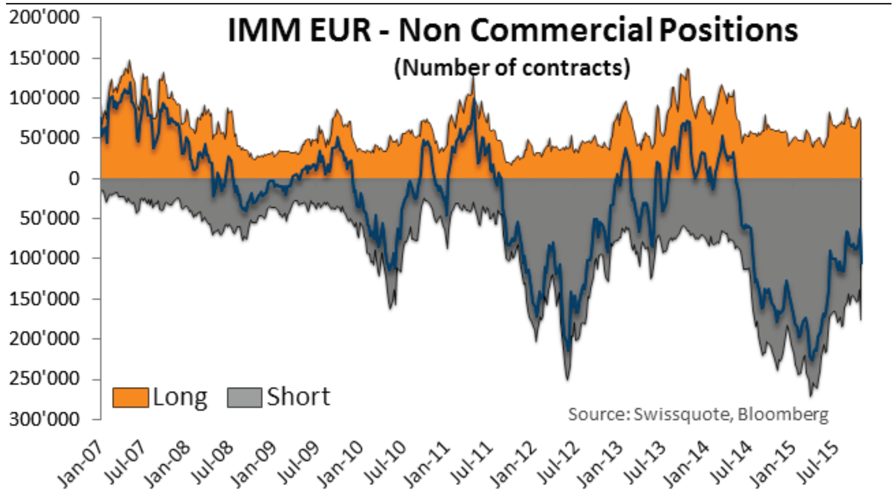
The International Monetary Market (IMM) non-commercial positioning is used to visualise the flow of funds from one currency to another. It is usually viewed as a contrarian indicator when it reaches an extreme in positioning.

The IMM data covers investors' positions for the week ending October 27th 2015.

Net long NZD positions have continued to increase substantially over the week ending October 27th, rising from from 12.47% to 17.61% of total open interest. However, we believe that the recent weak data from New Zealand will likely bring Kiwi bulls back to reality.

Net short EUR positions have increased substantially, reaching 27.84% of total open interest. Given the monetary policy divergence between the Fed and the ECB - Mario Draghi made clear that he was ready to support the EU economy further - we expect short positions to continue increasing.





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