WEEKLY MARKET OUTLOOK

29 February - 6 March 2016

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WEEKLY MARKET OUTLOOK - An Overview

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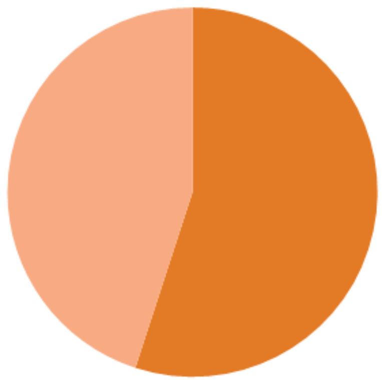
Economics

Brexit Mania Underway

The rhetoric and speculation around Brexit increase intensity this week. The GBP recovery rally was quickly squashed despite positive headlines following UK PM Cameron's renegotiated deal with the EU. The negative sterling sentiment was generated by news that London Mayor Boris Johnson announced his backing for leaving the EU. This move not only represents a well-known populist embracing a key issue but potentially a leader to an otherwise fragmented political movement. We continue to stress that this debate has only just begun. While headlines might suggest a direction, the result will only be known on June 23rd (or shortly after). Therefore, we would short any GBP rallies as downside is attractive as Brexit risk premia remains (despite extreme short GBP positioning). The EU referendum is a classic populist issue where logical arguments are less compelling than emotional responses. As we have seen with the current US republican presidential primary, appealing to irrational fears can sway voter's intentions. Should the pro-Brexit side mobilize and launch a targeted passionate campaign the expectations for a Brexit will increase significantly.

EURUSD has suffered from the realization that Brexit would fundamentally end the "ever-closer union." Broader contagion has been modest as 10-yr peripheral yields have barely budged. Yet, further significantly Brexit fueled FX weakness is unlikely. UK poll are notoriously inaccurate while the illusionary supportive "facts" supporting in-or-out will quickly get discounted by the opposition. Therefore neither side will make a strong advance. Yet, Eurozone economic data continues to show decelerated increases in the expectations for aggressive ECB policy accommodation in March. Expectation of additional stimulus will pressure Euro.

EU Referendum Vote Intention Poll of Polls (average six polls)



Source: www.WhatUKThinks.org

Economics

Mexico: Peso’s Weakness Is Not Over

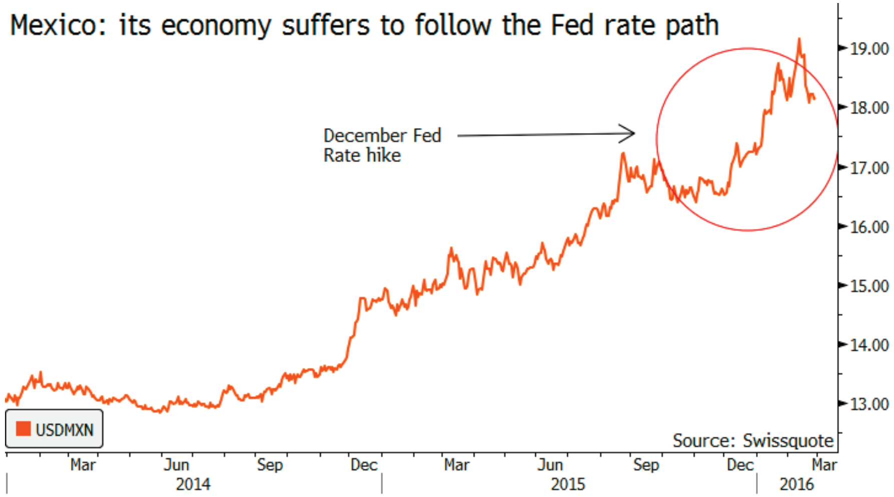
Oil industry suffers

The Mexican peso keeps struggling as it went from below 15 peso for one single dollar note early 2015 to above 19 a few days ago. Lingering low oil prices have contributed to weakening the currency as less revenues come from oil but it is also true that over the past twelve years, the share of total government revenue from the commodity has declined by one third to 20% from 34%. We firmly believe that there is one specific reason for this. Indeed, state-owned companies (including the main one PEMEX) have not been able to make sufficient investments. It has then prevented Mexico from gaining competitiveness over the past decade. The result of this policy is that Mexican infrastructure are now very antique. Now that crude oil is trading at very low levels, it seems obvious that Mexico must find another sources of revenue as investments on oil, which were already very low, have declined even more.

Recent data's weakness

Last week's data, current account balance, has been released and remains in deficit at around 8 billion dollar. Export revenues are clearly not sufficient to offset import needs. As a result, CPI jumped to 10-month high in early February. Regarding other data, Mexican's GDP is on the rise on the fourth quarter of 2015, but last December retail sales data printed negative at -1.6% m/m and industrial production has been also released at -0.1% m/m. Mexico is clearly suffering from the fact its central bank needs to carefully follow Fed's monetary policy (i.e. increasing rates when Fed is doing it) in order to avoid any capital outflow that may result from a narrowing rate differential. Mexico is way too dependent on the U.S. economy health which recovery is not sustainable yet.

Markets had also been closely watching the unemployment rate which will had been released at 4.30%. For the time being, it remains nonetheless to a six year-low. We consider that the unemployment rate may fall further. We are clearly bullish on the USDMXN which should head back towards 19.00.



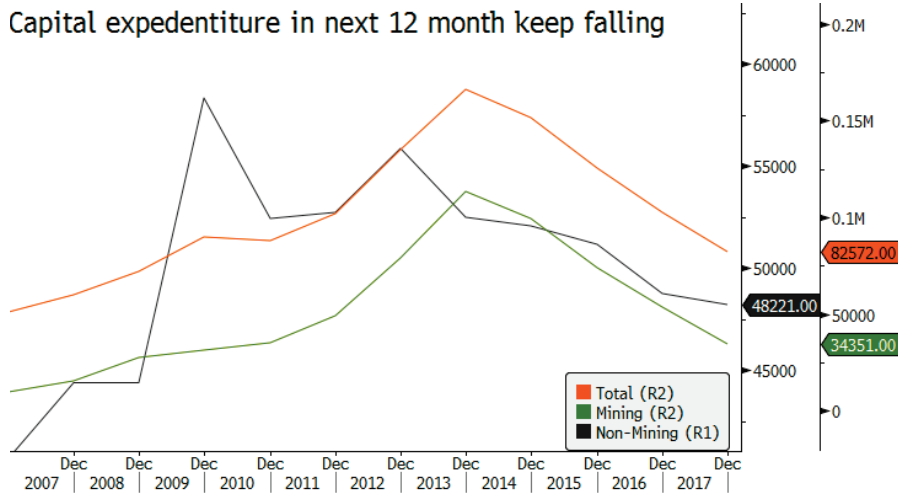
FX Market

AUD/USD Exposed To Downside Risk

The Australian economy started 2016 off to wheel as most economic indicators showed signs of stabilisation and even of improvement, for a few of them. The unemployment rate remained stable to 5.8% in December versus median forecast of 5.9%, while inflation pick-up significantly in the fourth quarter, rising from 1.5%y/y to 1.7% (beating estimates of 1.6%). However starting from February, a few cracks started to appear as the economy struggles to gain momentum in this low commodity price environment. Latest report showed that retail sales stagnated in December, while the market was expecting a 0.4%m/m rise. Both NAB business condition and business confidence indices decreased in January. Moreover, the unemployment rate rose to 6.0% in the first month of 2016.

According to the latest report from the Australian Bureau of Statistics released last Thursday, expected annual private capital expenditure fell sharply reaching the lowest level in nine years as Australian non-mining companies cut spending unexpectedly. The market was broadly expecting a collapse of investment in mining, mostly due to the prospect of low commodity prices and weak demand from China, but hoped that the non-mining sectors would compensate this setback. On the bright side, expected investments in manufacturing increased 9.3% for 2016-2017 compared to 2015-2017.

Overall, we believe that the pressure on the Aussie will increase substantially as the economy is losing momentum. Moreover, we expect the RBA to reiterate its call for a weaker Aussie at its next meeting on March 1st as Governor Stevens is most likely taking a dim view of the Aussie's recent appreciation. On Friday, AUD/USD was trading at around 0.7200 after failing once again to break the 0.7250 resistance area to the upside. In our opinion, the AUD/UD is greatly exposed to downside risk as both technical and fundamental analysis suggest a bearish reversal.



Economics

Russia Between Inflation And Recession

A weakening currency

The ruble keeps on suffering. The currency has strongly weakened against the greenback and is now trading around 76 ruble for one dollar. Recent fundamentals data shows that the Russian economy is struggling. Last week's Russian CPI has been released at 1.5% YTD. This data represents a major concern for the Central Bank of Russia as it does not leave much room for further easing despite a key rate around 11%. There is indeed a massive downside risk for the currency coupled with a major inflation risk. The country is definitely struggling with lingering low oil prices with the government adopting a budget based on oil prices at $50 a barrel. In addition 2015 growth rate fell at -3.7% y/y down from the slight rise of 0.6% in 2014.

As a result, the CBR is trying to stabilize the ruble by expanding its Foreign-Exchange reserves (including gold) and today, this amount for the period ending 19th of February will be disclosed. Russia's Central Bank head, Elvira Nabiullina has already made it clear that one of its primary objectives is to increase these reserve holdings up to $500 billion. For the time being, holdings only amount to $379.4 billion down from $382.4 billion a week earlier.

The importance of having gold

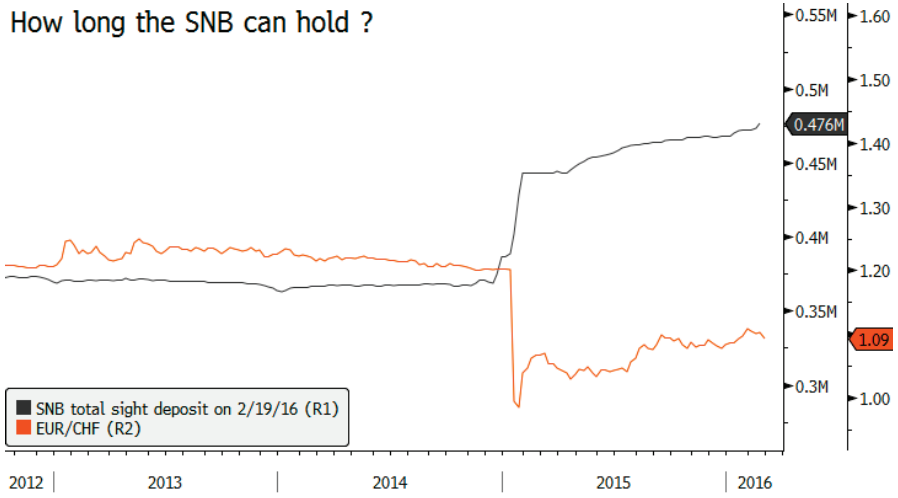
We consider that Russia needs more gold in order to gain credibility. Gold definitely represents confidence in a Central Bank. For the time being, price of Gold and Metals are improving and the last quarter was the best performing quarter for gold in the past thirty years. Gold is now trading at and are now back to a 1-year high. We truly believe that a disconnection between physical gold and paper gold will happen. Indeed, the ratio between the two becomes massive as there as now more than 200 times more ounce of paper gold that physical gold. This ratio as doubled in a few years. In our view, we remain bullish on Gold as there are growing evidence that the Fed will stay dovish for some more time and therefore it adds some upside pressures to metals' prices. And with lingering low interest rate coupled with threat of a possible QE4, Gold is definitely pushing higher.

Economics

SNB To Run Out Of Options

In the wake of Thomas Jordan's speech in Frankfurt last Tuesday, the Swiss franc came under renewed upward pressure as EUR/CHF moved below the 1.09 threshold for the first time since mid-January. One of the reason could be that the SNB's chairman delivered an unclear message about the limit of negative interest rate policy, while data from the euro zone came on the soft size. On one hand he warned the ECB about the potential negative effects of an excess use of unconventional measures, such as an excessively negative deposit rate - arguing it could trigger a flight to cash but recalled that it is a perfectly viable monetary tool. In our opinion, the problem is that the SNB is also implementing a negative interest rate policy, which is furthermore much more aggressive that the one of the ECB. The SNB is therefore also under the threat of a flight to cash and is far more exposed than the European Central Bank to this problem. It just like shooting yourself in the foot.

Even though Mr Jordan demonstrated that small neighbouring economies, such as Switzerland, Denmark or Czech Republic, weathered relatively well the recent turmoil - thanks to their aggressive monetary policy - we had the feeling that this lecture was an admission of weakness by Thomas Jordan as he suggested that cutting rate further into negative territory will come at a potential strong cost, while intervening massively on the FX market was almost out of the table given the SNB's willingness to hold its balance sheet to a manageable level. By making such statements Mr Jordan admits that the SNB has little room to act and is highly vulnerable to any monetary policy move from the ECB. Finally, the SNB chairman did not discuss its arsenal of policy tools. The reason for this may be that the SNB has no viable tools left in its bag and would rather try to convince the ECB to back off.

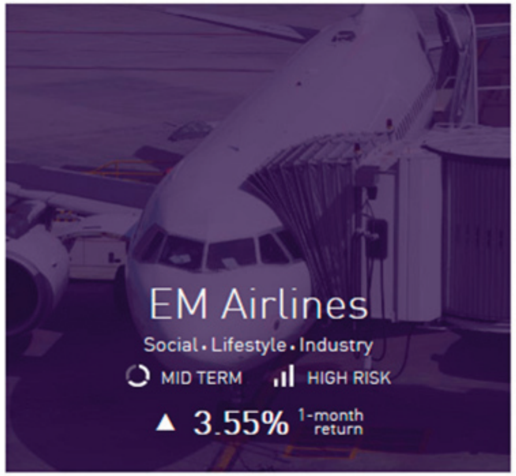


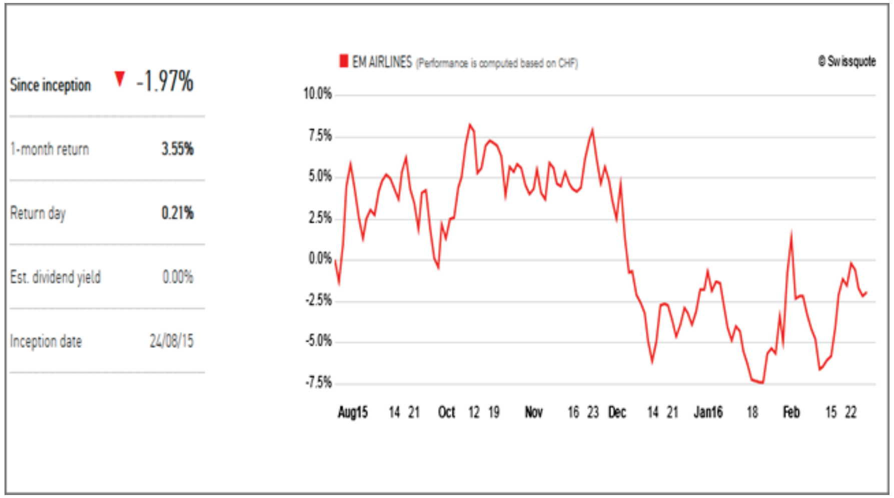
Themes Trading — EM Airlines

While demand for air travel is high globally, it is exploding in developing markets, and low-cost regional carriers (LCRCs) are taking advantage of this flourishing opportunity. Emerging markets are generally characterized by large populations and large geographical areas, and underdeveloped road systems make air transport the most efficient mode of travel. In addition, rapidly rising disposable incomes are making low-cost carriers accessible to a growing segment of the market. In Asia, 525 million people can be classified as middle class – more than the EU's total population. According to a major consulting firm, the middle classes are expected to expand by three billion over the next two decades, almost entirely in the developing world.

Airline industry revenues reached $746bn in 2014, with growth driven by low-cost carriers expanding in developing markets. The cost of airplanes has steadily declined, while low interest rates make for cheap financing to expand fleets. In addition, with fuel costs at a six-year low, airlines can pass savings on to consumers. The current growth of LCRCs is driven by evolving technology that helps carriers build stronger relationships with their customers, manage costs more effectively and sustainably enhance their financial performance. As developing markets expand, chances are that air travel will do so as well.

Analysis & Portfolio - Swissquote Bank Strategy Desk





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