SWISSQUOTE

WEEKLY MARKET OUTLOOK

4 - 10 April 2016

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

DISCLAIMER & DISCLOSURES

WEEKLY MARKET OUTLOOK - An Overview

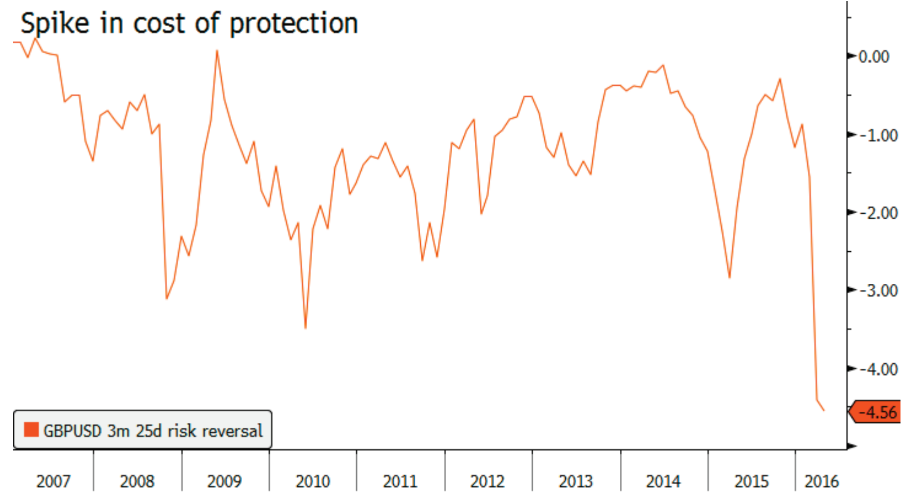
p3	Economics	Foreigners Sell UK Debt - Peter Rosenstreich
p4	Economics	AUD Subject to Downside Risk As Commodity Rally Falters - Arnaud Masset
p5	Economics	Lower Economic Activity For Mexico - Yann Quelenn
p6	Economics	China's Economy Responds To Stimulus - Arnaud Masset
p7	Economics	Loonie Continues To Move Higher - Yann Quelenn
p8	Themes Trading	Asia Gaming
	Disclaimer	

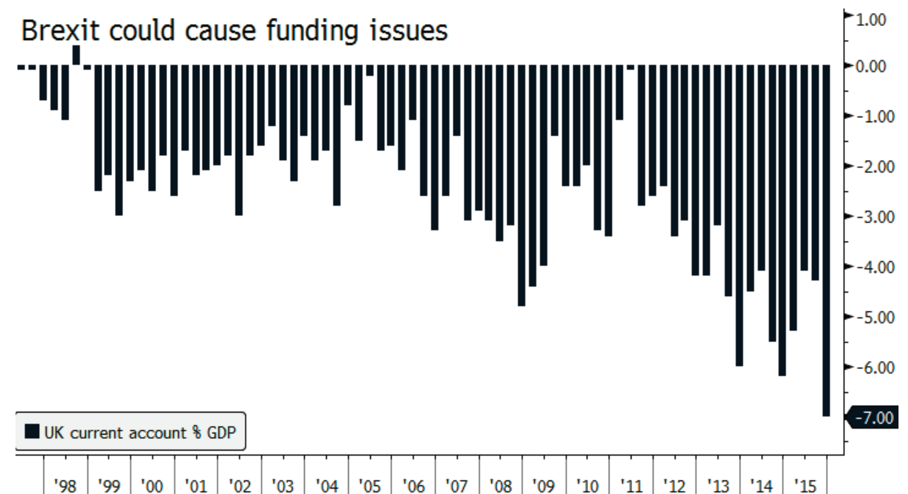
Economics

Foreigners Sell UK Debt

The broad risk rally has put Brexit fears to the side for now. However, spike in 3 month volatility (closest duration to the EU in/out vote) indicates that investors are quietly taking protection. Recent polls on the outcome for the EU referendum remain too close to call, increasing the probability that the UK could leave the EU. The average result of six polls indicated that "remain in" votes captured 51% of the vote while "leave" captured 48% of the vote. This week, the BoE listed the risk of a Brexit at the top of near term threats to financial stability. Highlighting the expectations for the BoE to step in to control, Brexit generated volatility. Forward contact based on Sonia index are pricing in an interest rate cut by years end.

Last week soft UK economic data highlighted the weakness in sustained Brexit uncertainly. UK current account deficit reached an all-time high as foreigners cut purchases of gilts and reduced earnings from abroad by UK companies. The Brexit debate is highly centered on the UK huge current account deficit as tightening in lending from abroad (yet upwards revision to borrowing for the next three years) suggests that slack will be need to be picked up by domestic public sector. With steady public sector deficit unlikely to normalize anytime soon, there is a risk that private sector investments will need to drop in order to fill in gap. With less participation by the household consumer, there should be considerable drag on growth near-term. Further reduction in capital inflows into the UK will weigh on the GBP. Elsewhere, March manufacturing PMI disappointed at 51.0 verse 51.2 exp. The fall in sentiment confirms worries over the 23rd June EU referendum as businesses have increasingly become cautious in regards to spending and hiring decisions. We remain negative on the GBPUSD, watching for a continued reversal of bullish momentum targeting 1.4100.





Economics

AUD Subject to Downside Risk As Commodity Rally Falters

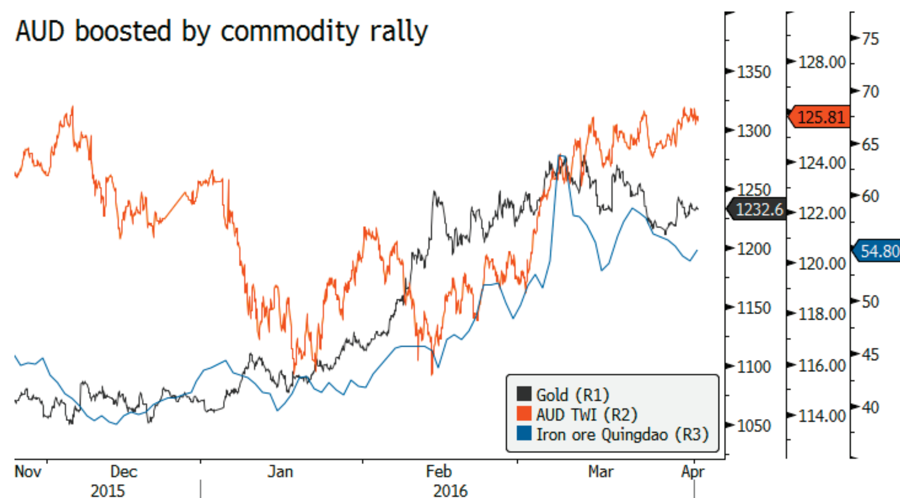
Commodity rally pushed AUD

Global economic conditions were rather favourable for the Australian dollar in the first quarter as commodity prices rallied, while the US Central Bank started the year on the back foot; forced to delay further rate increases. Moreover, the price of Australia's top export commodity, iron ore, has risen massively over the last few months. The price of a metric ton for delivery at the port of Qingdao rose as much as 66% from December's low to $63.70 on improving prospect for China's economy. In the end, it stabilised at around $55. Gold was also one of the best performing assets of 2016, rallying from $1,051 an ounce in early January to $1284 on mounting uncertainties about the global economy. Finally, crude oil prices rallied substantially with the WTI surging more than 50% to roughly $40 a barrel. As a result, traders rushed to get loaded on the long side of commodity currencies, pushing the Aussie to a multi-month high against the US dollar.

Iron ore price set to adjust lower

However, we believe this euphoria is coming to an end as the fundamentals simply do not justify further appreciation of commodity prices, especially iron ore. Firstly, China's iron ore port inventories have been rising steadily since July last year and reached 94.8 million tons for the week ending March 25, while crude steel production kept decreasing, reaching 58.5 million tons (as of February 29) amid weak steel demand. Indeed, China's construction sector, which is the largest consumer of steel, continues to slow down due to the housing glut, and the outlook does not look great. Taking all those elements into account, we believe that iron ore prices have only one direction in which to go: downwards.

The rally in the Australian dollar already started to show signs of weakness as commodity prices entered into a period of consolidation, if not of correction. Gold fell roughly 2% through the course of March, iron ore prices slipped 3.50%, while crude oil stabilised below $40 a barrel. All in all, the commodity price stabilisation will most likely translate into a correction of the Australian dollar - or at least a consolidation. We do not rule out further Aussie strength in the short-term but we believe that a correction is bound to happen.



Economics — Lower Economic Activity For Mexico

Breathing space with higher oil price

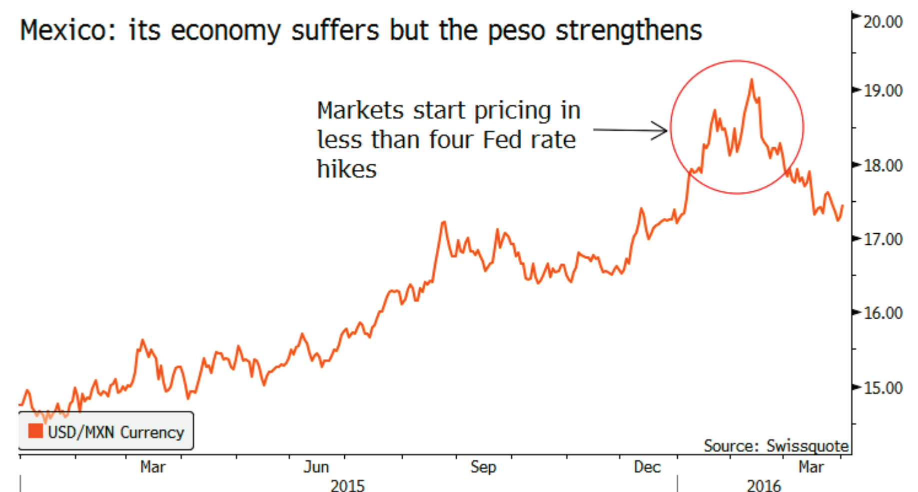
Last week, January economic activity data have been released lower than expectations at 2.33% m/m, and also lower than in December when it came in 2.56% m/m. It confirms the underlying difficulties of the Mexican economy which is highly dependent on the United States and oil exports. The collapse of the black commodity is still having an important impact on the country. Yet, current rebound is a good news for a country that still lies on the shade of its big neighbour.

In the Fed's path

Mexico's curse is that its central bank needs to carefully follow the Fed's monetary policy in order to avoid any capital outflow that would result from a narrowing rate differential. In 2015, the Mexican central bank changed the dates of its interest-rate decision based on the FOMC's meeting dates in order to be more reactive to any change in US monetary policy. In other words, it wants to ensure it can respond to an increase in US borrowing costs.

Oil price is still too low

It is clear that in the event of a rate hike, Mexico's economy will be at stake as the country continues to pay the price for its lack of investments in its industry sector, in particular its oil industry. In addition, extracting the Mexican oil is expensive and the breakeven price is still above the current market price. On top of that, with an out of date infrastructure the country simply does not have a fighting chance to compete in the oil market. Nevertheless, we believe that the health of the US domestic economy is overstated and believe that no further rate hike will happen this year. The dovish stance is clearly retreating and unfortunately for Mexico, we should therefore see additional weakening in the USDMXN. As a result, the Mexican GDP is set to suffer.

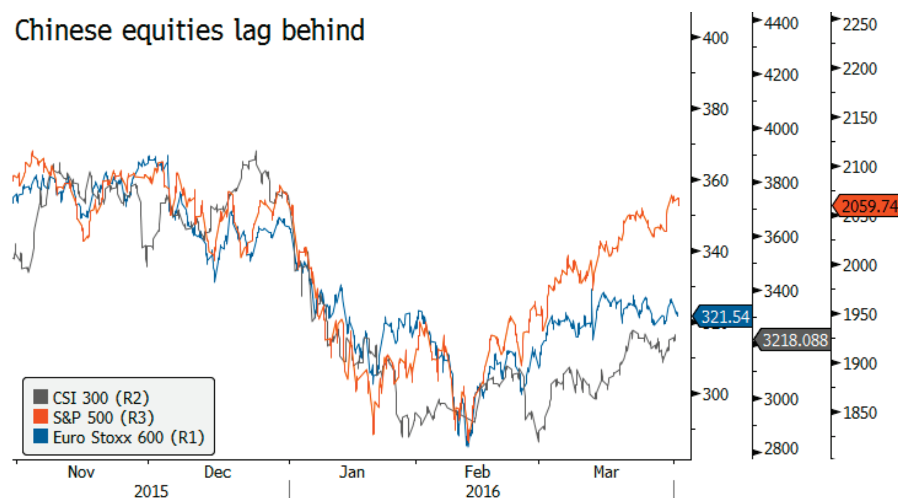


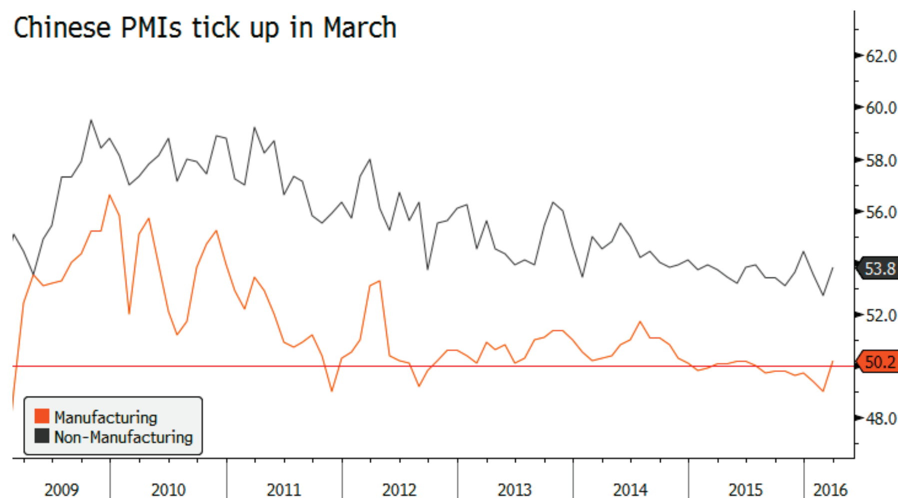
Economics

China's Economy Responds To Stimulus

Last Friday, the last batch of data from China sent mixed signals to investors. Chinese manufacturing PMI surprised massively to the upside, suggesting that the effects of the several rounds of easing undertaken by the PBoC, together with the government's fiscal stimulus did actually help the economy to adapt to the "new normal" of slower growth. The official manufacturing PMI passed the 50 mark that separates growth from contraction, printing at 50.2 in March from 49 in February (also beating median forecast of 49.4). Looking at the details, the improvement was mainly due to an increase in output, new orders and new export orders. Similarly, the non-manufacturing PMI rose to 53.8 from 52.7 in the previous month. However, according to private data, the manufacturing sector is still in contraction as the Caixin manufacturing PMI printed at 49.7, beating consensus of 48.3 and the previous month's reading of 48 but still below the 50 threshold.

However, this good news, which should be viewed cautiously due to the strong seasonality effect of Chinese New Year, has been overshadowed by the downward revision of China's credit rating by Standard & Poor's from stable to negative. Though this news did not come as a surprise, it still sent a negative signal to investors, reminding them of just how much remains to be done in the fiscal adjustment field to prepare for the new weak global demand environment. Over the last few months, the market has been lost, not know where exactly to stand as the effect of the PBoC and government stimulus took time to show results. This has translated into trendless trading for Chinese equities, while global equities exhibit strong gains during the March quarter.





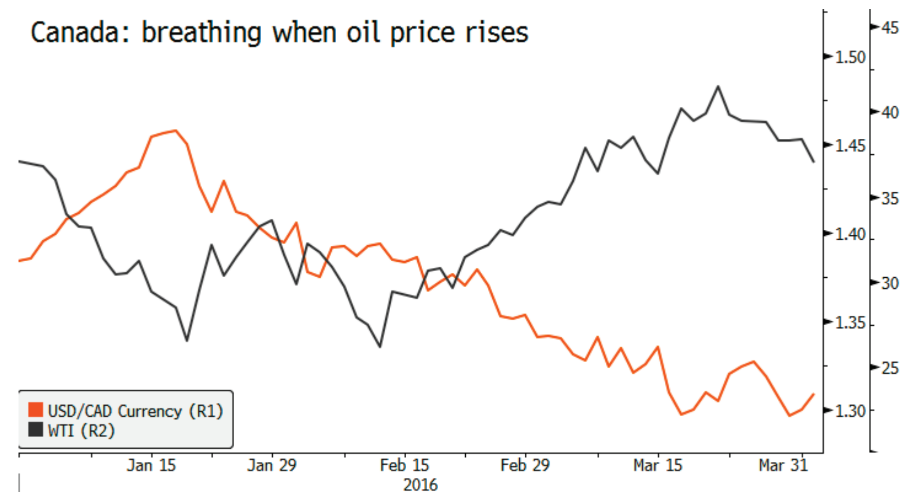
Economics

Loonie Continues To Move Higher

Crude oil prices are now stabilising and providing some relief to the loonie with most Canadian revenues depending on the black commodity. Yet, the currency is still trading at low level around 1.3000. Earlier last week, January's GDP data have been released. Data came in above expectations with a print at 0.6% m/m, above prior December data at 0.2% m/m. The Canadian economy has strengthened for the four consecutive month and it is the strongest GDP release since July 2013.The strong number has been mostly led by manufacturing and exports, along with industrial production which is up 1.6%.

However, since January, overall economic conditions have evolved and GDP's data do not reflect the commodities improvement. Crude oil prices have sharply bounced and gold surged. As a result, we do believe that the Canadian economy is going better and that a sustainable recovery is happening. The chance of a further rate cut at the next monetary policy meeting is getting lower. Even better, we consider that the Bank of Canada should not cut rates this year. Last year's slump in oil prices had compelled Canadian policymakers to cut rates twice. For the time being, it seems that it gained some more rooms in case of adverse economic conditions.

Currency-wise, medium-term pressures are bearish on the USD/CAD. Indeed, key drivers of the pair remain mostly commodity prices and U.S. monetary policy. As we continue to reiterate, the Fed rate path was largely overestimated and instead of four rate hikes, markets have only priced one or two. With this in mind we believe that financial markets still have to appraise the weakness of the US economy and in our view no further rate hike will take place this year. As a result upside pressures on the loonie are set to continue. We target an exchange rate of 1.2900 for the USD/CAD over the short-term.

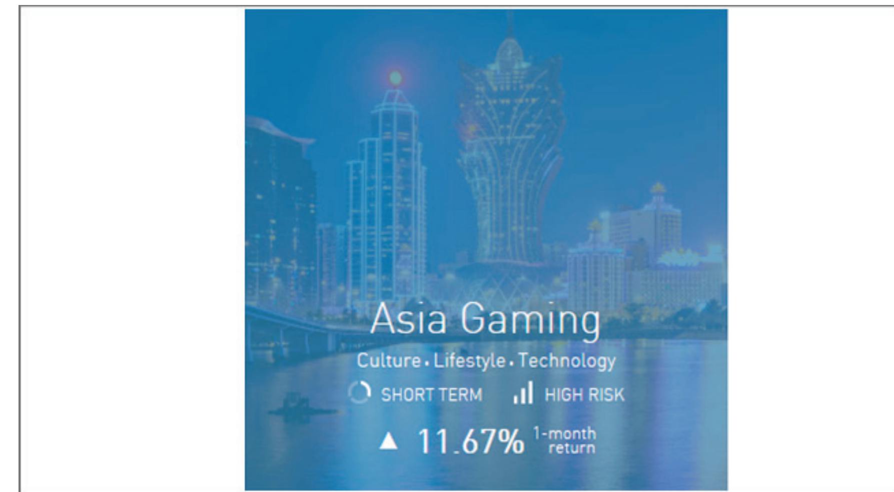


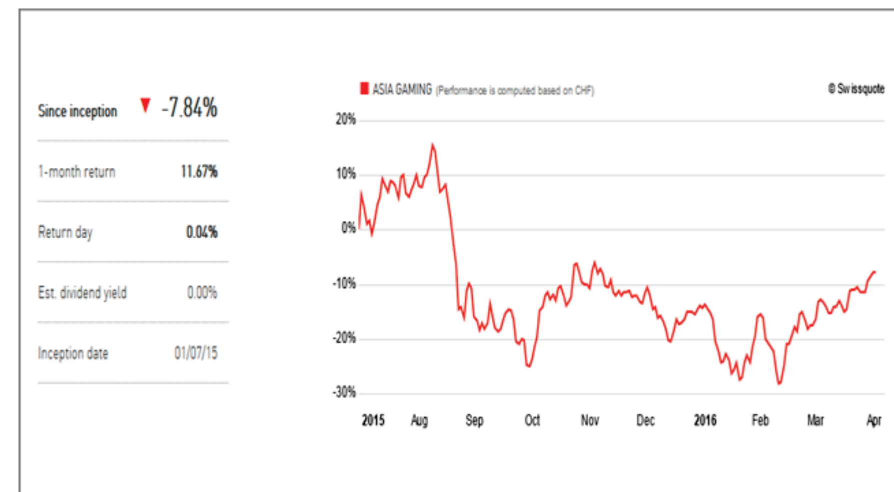
Themes Trading — Asia Gaming

Like playing poker for money, investing in the global gaming industry has always been a risky business in which both skill and luck are needed to win. Yet despite negative press over the past five years, the industry has seen compound annual growth of over 9% and, according to projections, 2015 casino gaming revenue should reach $182 billion. Within this dynamic industry, no region has shown stronger momentum than Asia, as the hunt to tap into the world's largest migration of wealth has led to rapid expansion in casinos and casino hotels. The recent regional economic slowdown and regulatory uncertainty have eroded the earnings outlook and valuations.

Macau's gross gaming revenue is highly correlated with Chinese GDP growth, which has slowed considerably. However, with evidence suggesting that the Chinese government intends to engineer GDP growth and reflate the economy, we foresee a recovery among the region's casinos. In an effort to grab a slice of the newly well-heeled mass market, Asian casinos are shifting their focus away from pure gaming revenue towards more family-friendly destinations. In addition, gaming stocks have historically behaved counter-cyclically, suggesting that mass-market gaming ought to be less affected by the economic climate.

We created this theme by filtering on regional Asian stocks that generate over 50% of their revenue from casinos and casino hotels, screening out online gambling, race tracks and gaming services.





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. © Swissquote Bank 2014. All rights reserved.