# WEEKLY MARKET OUTLOOK

## 20 - 26 June 2016

DISCLAIMER & DISCLOSURES

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# WEEKLY MARKET OUTLOOK - An Overview

# Economics

# "Brexit" In Focus

**"Brexit" currency trades**

Shifting market expectations for Brexit is now a daily occurrence and we expect the noise to reach deafening levels next week. Yet, barring ironclad polling evidence of a directional outcome, we suspect investors will view the vote as coin toss. Intraday volatility, indicated by a surge in GBP option premiums, will likely remain elevated but we suspect that positioning close of Friday will last until morning of Thursday 23rd. We remain focused on a "leave" vote since that will likely have the most profound and confusing effect on currency prices.

Our primary currency trades on a "leave" vote would be short GBP/JPY and short EUR/CHF. Both the UK and Europe stand to lose should their relationship deteriorate with the possibility of the single currency rising above the sterling. Second tier trades would be focused on selling currencies with significant exposure to trade with both nations as we anticipate a contraction in growth due to immediate uncertainties. This puts NOK, PLN and SEK at risk. In this current scenario, we doubt counter factors such as safe-haven status and correlation to oil prices will protect SEK and NOK from an immediate sell-off.

Finally, we are focused on global risk sensitively where MXN, TRY and ZAR look to be the most vulnerable to a risk-off result. ZARJPY remains below its 21d MA at 6.8485, suggesting a test of the 6.5247 2016 low. As we have stated before on the long side nothing clever but traditional safe-haven USD, JPY and CHF. However, a fear of "Brexit" has once again also put bitcoin/cryptocurrencies back in the spotlight. Bitcoin against USD has surge to 777.01 (bitcoin/sterling 519), representing a two-year high. Cryptocurrencies in theory are the only pure way of escaping the manipulation of fiat currencies, and avoiding the potential distortion caused by central banks in the post UK vote environment.

**Referendum Schedule**

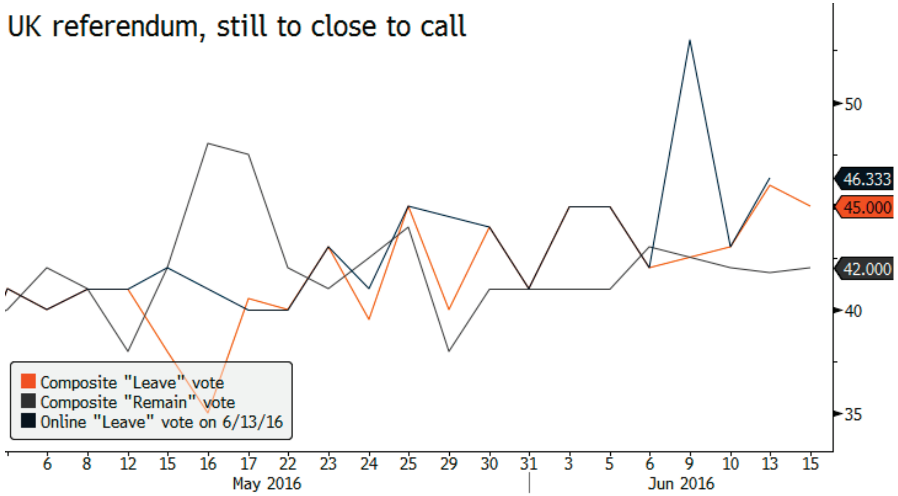
23rd June 07:00 – 22:00 : Polls are open (no official exit polls or unofficial polls can be published)

23rd June 22:00 : Polls are closed and 12 regional polling central will being counting votes

24th June 00:30 : Estimated release of first results from regional polling centers (results will be rolling)

24th June 06:00 : Estimated release of official results from 12 regional polling centers (Official declaration of result by PM Cameron soon after)

*times are BST (London time)



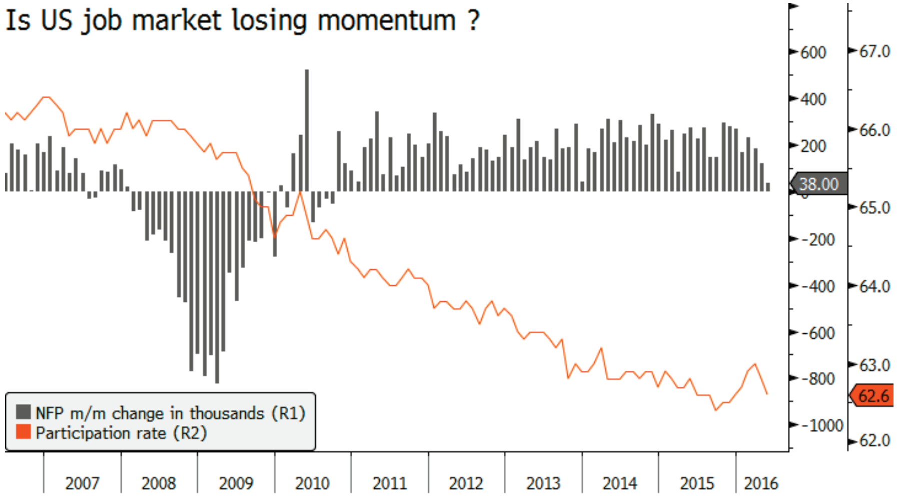
## Economics

# Cautious Fed Lowers Rate Path

The Fed released its interest rate decision last Wednesday. The tone of the statement and the press conference were roughly in line with expectations, meaning that the Fed maintained its optimistic view on the US economic outlook, while referencing the weak jobs data for May and the Brexit situation as sources of risk. During the press conference, Fed chairwoman Yellen made clear that more positive signs are required before lifting rates, stating: “We do need to make sure that there's sufficient momentum”. A cautious approach continues to prevail.

The Fed also updated its forecast, with growth projections being revised lower to 2% in 2016 from 2.2% at the March meeting. The unemployment rate is expected to stay at 4.7% by year-end, while inflation forecasts were revised higher. Personal expenditure is expected to reach 1.4% by the end of 2016, while the Fed’s preferred measure of inflation, the core PCE, is expected to reach 1.7% this year compared to 1.6% at the March meeting.

Looking at the dots, only two Fed members are expecting more than two rate hikes by year end compared to seven in March. Even though the median forecast is still on two hikes for this year, most members lowered their projections for this year as they realised that economic conditions do not allow an aggressive path. We maintain our bearish view that the Fed will not be able to lift rates more than once this year and this is our more optimistic scenario. Indeed for now the global environment is not conducive to any monetary policy tightening as central banks across the planet continue to ease further their monetary conditions. Therefore if the Fed persists in going against the flow, the subsequent strengthening of the US dollar could derail the fragile ongoing recovery.



## Economics — Unsurprisingly SNB Kept Rate Unchanged

### SNB and FOMC opt for status quo

A week before the Brexit referendum and a day after the FOMC meeting which has seen the US rates being unchanged as widely expected by financial markets, the SNB announced its deposit rate decision. The Swiss institution has decided to keep it on hold at -0.75%. It is clear that the SNB is waiting for the Brexit Referendum result before taking any further action. Indeed, the stability of the country would be at stake as Switzerland is way too small to be a leader in the monetary policy. It cannot drive financial markets. It can only be reactive to what is happening globally. On top of that the SNB is not willing to set again a minimum exchange rate. This strategy has proven to be too costly.

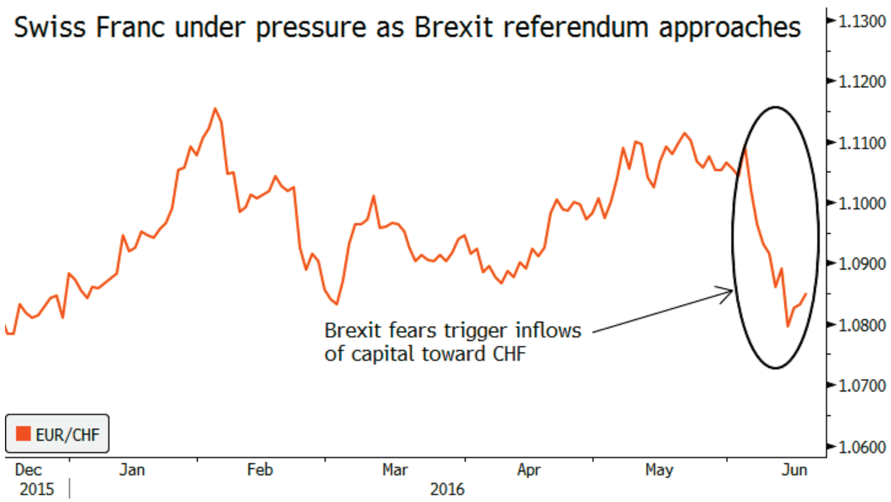
### Swiss fundamentals are improving according to the SNB

For the time being, the Swiss domestic situation is still manageable despite the data are either mixed or on the soft side. Inflation is slightly picking up with the last four monthly figures printed positive, last May data showed a slight increase at 0.1% m/m. Nonetheless consumer spending remains fragile. GDP for the first quarter 2016 has shown only a 0.1% q/q increment and decelerates from Q4 2015 where GDP growth printed at 0.4% q/q.

Nonetheless Swiss policymakers consider that this is not an indication of slowdown. At the press conference following the rate decision, Thomas Jordan, Chairman of the Governing Board of the SNB, said that the central bank is confident about growth to climb for the second quarter of this year. He also mentioned that the inflation should rise at a quicker pace, over the next quarters, than what was predicted by the SNB in March regarding the surge in oil prices since the start of this year. For 2017, inflation is expected to progress by 0.3% and 0.9% in 2018. Out of this sluggish outlook the SNB will continue using negative interest rates and FX intervention.

### A Brexit may trigger a reaction from the SNB

However we also know that the central bank has a recent history of intervening out of usual SNB meeting and its interventions may likely be not expected in order to be as efficient as possible. For example in case the Brexit "Leave" vote wins, the inflow of money which is already very important towards the CHF will continue growing and force the SNB to react. At the moment, the EUR/CHF is getting weaker and is trading around 1.0800 for the first time in the last six months.



# Economics

## Brazilian Real Immune To Local Developments

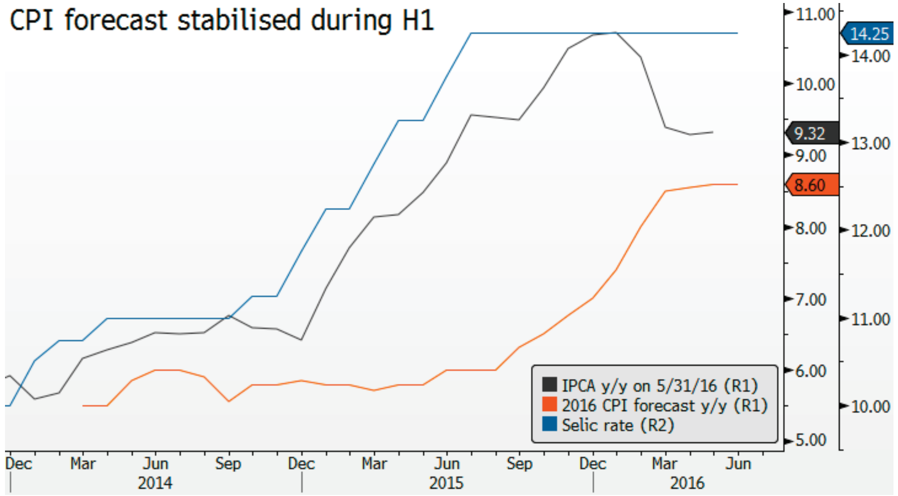
The Brazilian real had a bumpy ride over the last few weeks as investors switched from risk-off to risk-on mode ahead of last week's FOMC meeting and next week's Brexit vote. In fact over the last few months, the development of Brazil's political situation had only a small impact on USD/BRL as investors have little visibility over the political outcome and more specifically whether the new government will in fact be able to pass the necessary measures aimed at putting the country back on a growth path.

The task won't be easy for Brazil's interim president, Michel Temer, as he is facing corruption accusation (sounds familiar?). However, the government managed to launch a proposed constitutional amendment aiming at freezing future public spending in real terms in an attempt to address the fiscal deficit. Even though it seems to be a good solution, the lack of details about how it would implemented - i.e. what is going to be cut - has left investors doubtful. For now it is just words. In the meantime, investors focus on international developments and put the Brazilian situation on the backburner.

Even if the Brazilian situation is messy for now, investors have begun to be more optimistic about the outlook. Economists have revised their growth forecast for 2016 to the upside from -3.88% in early to -3.60% last week. The current account deficit has also been revised downwardly to $15.20bn from $20bn.

All in all, the storm clouds seem to dissipate in Brazil but the uncertainty stemming from the political turmoil, which could potentially last until November - the Senate has 180 days to conduct a trial - has kept investors cautious. USD/BRL will therefore continue to be driven by international development as investors will focus again on the Brazil political situation once they get better clarity on the Brexit and US rate hike stories.

CPI forecast stabilised during H1



# FX Markets

## IMM Non-Commercial Positioning

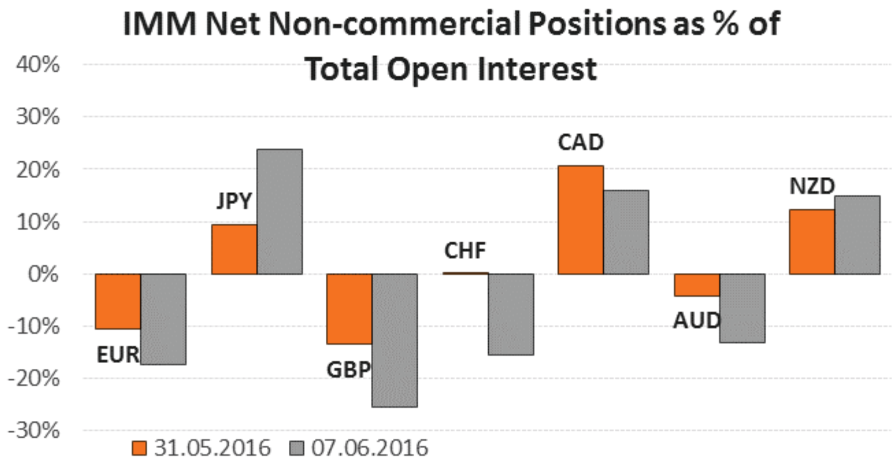
**The International Monetary Market (IMM) non-commercial positioning is used to visualise the flow of funds from one currency to another. It is usually viewed as a contrarian indicator when it reaches an extreme in positioning.**

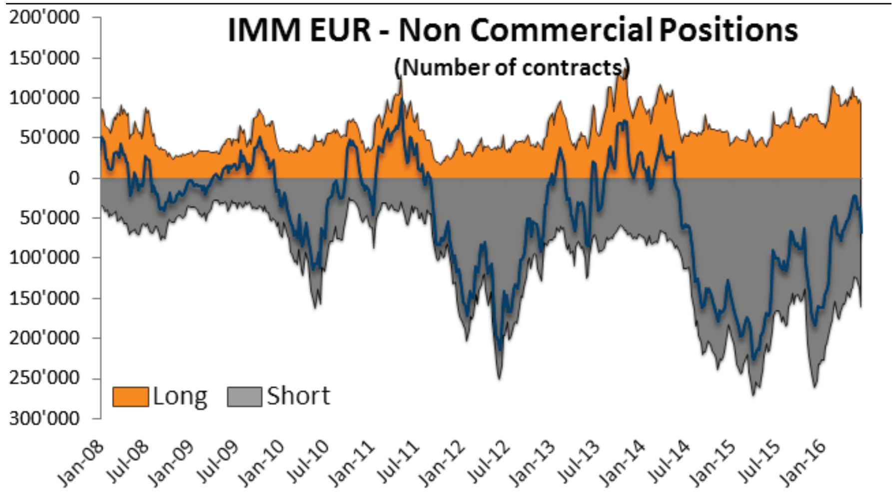
The IMM data covers investors' positions for the week ending June 7th 2016.

The EUR net position is shorter as the Brexit is approaching and the risk-off sentiment dominates. The net position for the GBP is also shorter which can be easily explained. Indeed, there is an important downside risk for the currency in case the "leave" vote wins next week.

Despite verbal intervention from the BoJ which may add further stimulus before the end of the year, the JPY currency still serves as safe haven in this risk environment. The net position is clearly long.

Speculators have decreased their long position in CAD as oil price has, for the time being, stopped its medium-term bullish move.



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