WEEKLY MARKET OUTLOOK

1 - 7 August 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

WEEKLY MARKET OUTLOOK - An Overview

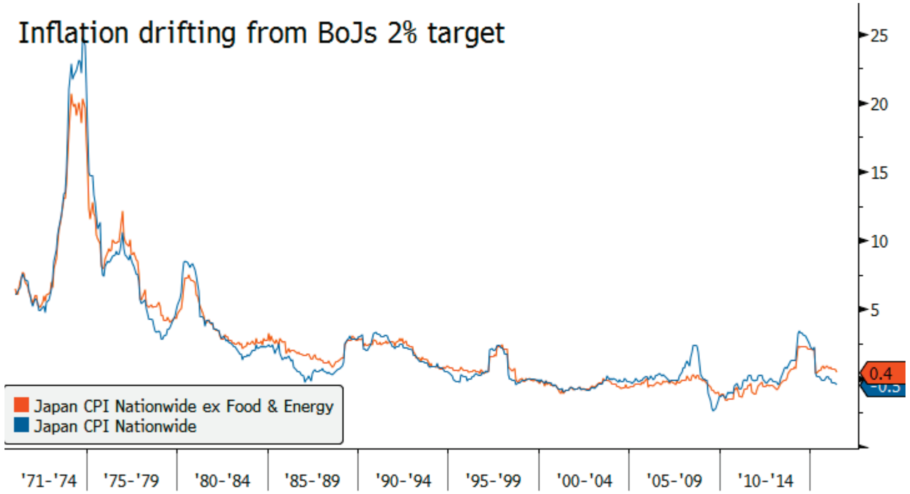
Economics

BoJ Policy Announcement Disappoint

After significant hype the BoJ disappointed the market by not cutting interest rates or expanding its monetary policy base (keeping interest rates at -0.1% and JGB purchases at 80trn per year), but instead choose a timid broadening of the current policy mix. The BoJ expanded its annual ETF purchase program by JPY3trn to JPY6trn. This represents approximately 1.6% of Japan's equity market float, providing Nikkei with solid support. However, the JPY strengthened across the board as the realization that deeper stimulus was not imminent, spread across the market. The strong JPY indicates that the Nikkei is likely to lose gains next week. While the BoJ conducted non meaningful micro turning, the government was preparing to launch an agrressive policy package. Prior to the BoJ decision, Chief Cabinet Secretary Suga stated that the upcoming stimulus package would be approved August 1st, which will be good news for corporates but not JPY. The scope and size of the economic package has already been widely circulated by the media, therefore market impact is unlikely.

In our view, Japan is now shifting away from monetary to fiscal easing as the effectiveness of current policy has been challenged. BoJ and Governor Kuroda has announced it will conduct a "comprehensive assessment" of policy effectiveness at its September policy meeting. This gives the BoJ and investors nearly two months to figure out what Japan's next steps might be and their potential effectiveness. The "comprehensive assessment" of policy gives members time to review “helicopter” money which we suspect remains on the table. However, the failure by the BoJ to excite the markets highlights a growing theme of central bank policy incapability which should have pronounced implications in early 2017.

USDJPY continues to be heavily influenced by BoJ / Fed policy expectations. With BoJ running out of ammo, fundamental drivers of JPY strength stable, and Fed unlikely to move before the winter, downside to USDJPY looks attractive.



Economics

AUD Subject To Downside Risk Ahead Of RBA Meeting

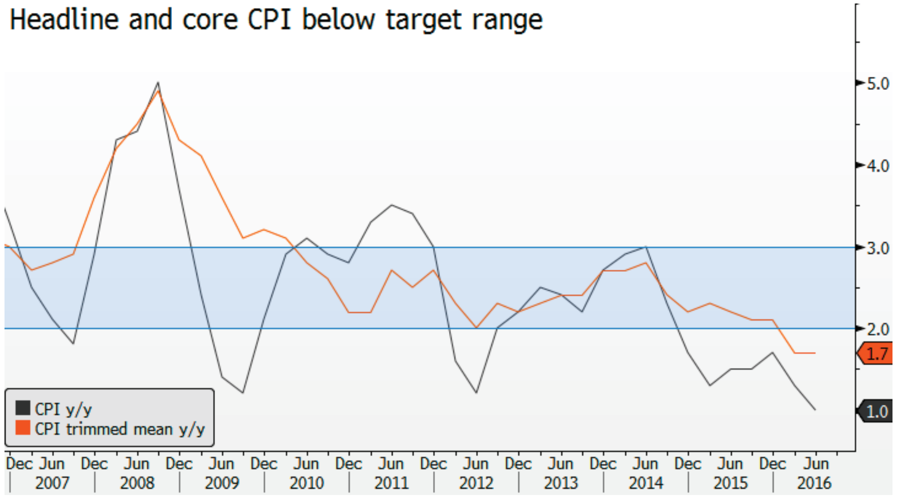
Weak inflationary pressures

The latest inflation report from Australia came in on the soft side but was still better than anticipated by economists. Headline CPI rose 1.0%y/y or 0.4%q/q in the June quarter - the lowest level in seventeen years - roughly matching the median forecast. On the bright side, the RBA's preferred measure of inflation - the trimmed mean, which excludes the highest rises and declines among CPI components - massively surprised to the upside. It rose 0.5%q/q (0.4% exp. and 0.2% in 1Q) or 1.7%y/y (1.5% exp. and 1.7% in 1Q), clouding the issue of the next RBA rate decision on August 2. In addition, released on Friday, producer prices grew only 1%y/y in the second quarter from 1.2% in the previous as import prices fell further.

RBA to cut rate

Indeed, even though the inflation report is far from being encouraging vis-à-vis Australia's inflationary outlook, it does take some heat off the RBA, giving more room for Governor Stevens to delay a potential interest rate cut next Tuesday. From our standpoint, the CPI report does not change much in the RBA's thinking as the overall trend in inflation is negative; and the latest uptick suggests, at most, a stabilisation and not a reversal yet. Moreover, the Fed's inaction will likely nudge investors towards higher yielding currencies such as the Aussie and the Kiwi. Therefore we expect that the RBA will cut the cash rate target in order to ease the buying pressure on the AUD and to bring core inflation within the 2% to 3% target band. Consequently, the Australian dollar still has downside potential and should resume its debasement towards the $0.73 level as a first step.

Headline and core CPI below target range



Economics

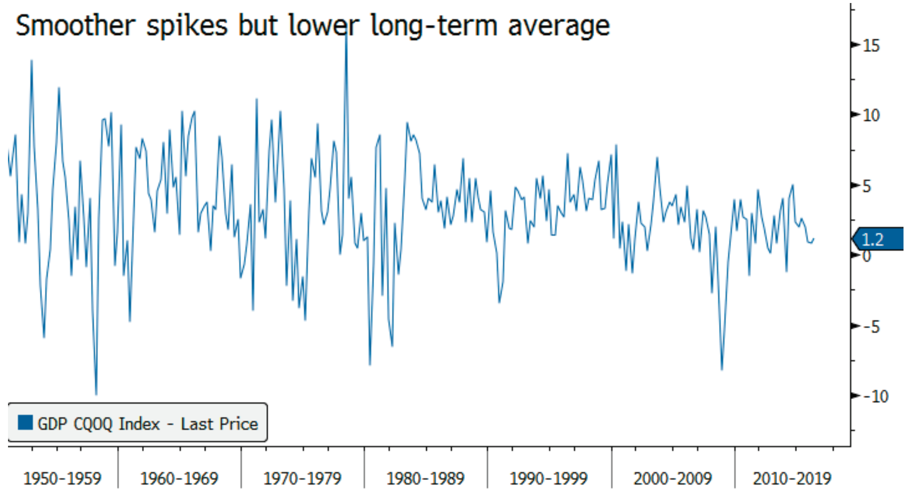
Summer heat creates “September” hike delusion

The combination of summer heat and long days sometimes produces a mirage effect, making investors see things that are not there. This is case-and-point with yesterday's Fed rate decision and accompanying statement. The Fed held policy unchanged and provided, in our view, a statement in line with expectation. Rumors of a hawkish statement are delusional. The inclusion of the wording "near-term risks to the economic outlook have diminished" are referred by some to predict a “live” September meeting. However, we and the markets remains skeptical that risk contracted, but rather increased, especially with the Brexit vote and impending US presidential election.

The FOMC concerned over weak fixed investment and low inflation expectations will undermine solid job markets and volatile household spending. The incoming US data is decent but hardly rate hike worthy and the Fed has little to gain with raising rate to early (in fact a September rate hike and resulting stock market crash would likely give Republican Trump the US presidency). While backwards looking GDP increased a limp to 1.2% in 2Q from 1.1% as personal consumption increased less then expected. Core PCE eased to 1.7% from 2.0%. So with no real inflation on the consumer or wage level, and growing concerns about sustainability, the Fed will stay on the sidelines.

The USD has been under significant selling pressure in the wake of the publication of the July FOMC statement. Even though the idea of a rate hike in September gained support to some extent, the market is still not pricing it in as US data does not allow us to see any significant trends in inflation and economic activity.

The current futures market is pricing in a 29% probability of an increase in the Fed funds target rate at the September meeting versus only 9% a week ago. Indeed, the Fed is more than ever in data dependent mode, meaning that the most hawkish Fed members will throw bullish comments at the first chance they get. We remain bearish on the USD, especially against EM FX as expectations for a September hike remain low. In addition, rally in US front- end treasury yields looks unsustainable.

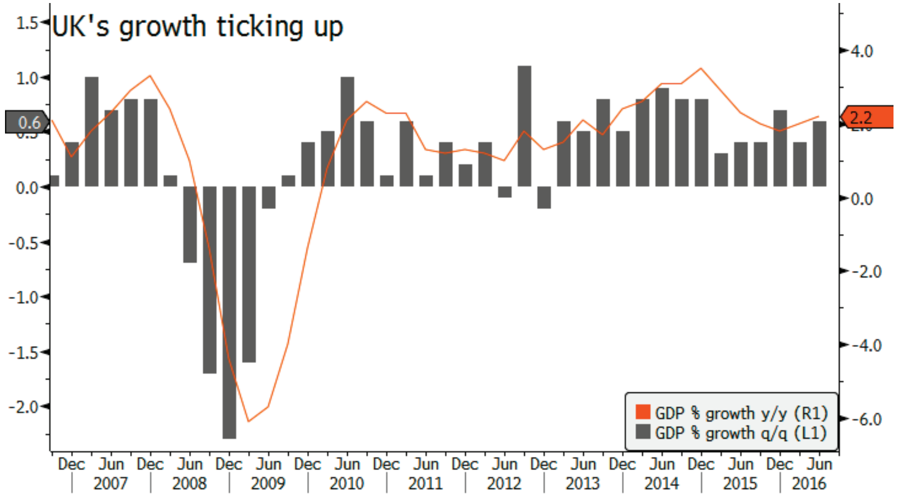


Economics

Stay Short GBP Ahead Of BoE Meeting

In the wake of the Brexit vote, the BoE decided to back away from an immediate response, preferring to wait for the smoke to clear before using its last remaining ammo. Indeed, the BoE will only be able to cut interest rates a couple of times before reaching negative rates. However, we do not believe the BoE will further ease its monetary policy next week as the available data did not suggest a substantial deterioration of the UK economy since the July meeting. Inflation data surprised to the upside in June with both the headline and the core measure ticking higher. GDP figures released yesterday were rather encouraging, showing that the UK economy grew 2.2%y/y in the second quarter, beating estimates of 2.1% and above previous quarter readings of 2.0%. Therefore, it will take more than a grim PMI read (sharp contraction in all three of the PMI measures in July) and a weak consumer confidence index (-12 in July versus -8 expected and -1 previous) to trigger a rate cut.

The Bank of England has limited room for manoeuvre before switching to negative interest rates. Therefore, we expect the central bank to leave its benchmark rate unchanged at its next meeting on August 4th, waiting for further information about the implication of Brexit for the UK economy. On the other hand, the BoE could increase the target for asset purchases without cutting rates, which would give time to the institution to gather data, while still providing a fresh boost. GBP/USD spent most of last week treading water as investors were trying to grasp the ins and outs of the Brexit vote.

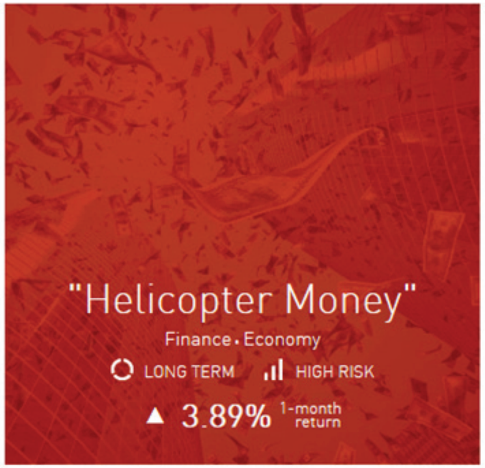


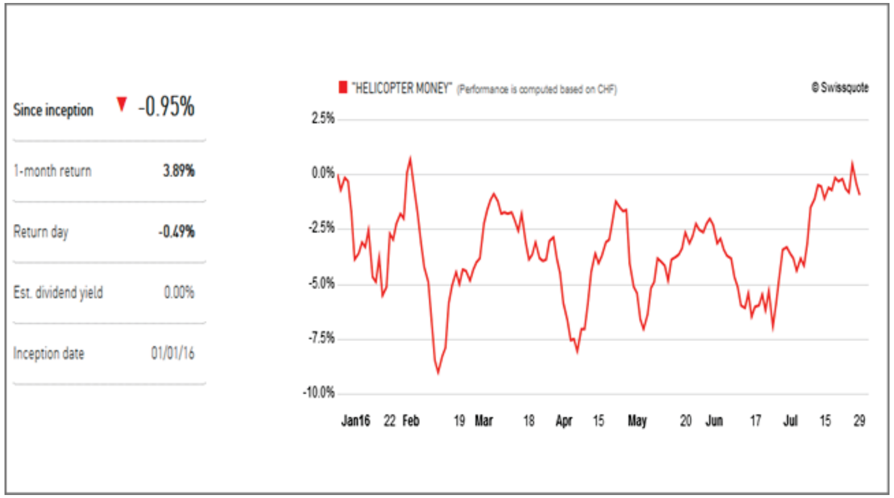
Themes Trading — "Helicopter" Money

"Helicopter money" is a monetary policy strategy that was unthinkable only a few months ago. However, after nearly ten years of dramatically unorthodox monetary policy by global central banks to escape stagnation, there is speculation that the Bank of Japan is considering the most extreme policy measure possible.

In an effort to end Japan's 20-year depression, Prime Minister Shinzō Abe launched an aggressive strategy dubbed "Abenomics." The Bank of Japan shifted into ultra-accommodative gear with negative interest rates and launched a massive quantitative easing package. The initial impact was positive, with Japanese growth and inflation both improving. However, the economic rally was short-lived, so the BoJ expanded the scope of its asset purchases to include bonds, ETFs, J-REITs… basically any liquid asset. Having exhausted all other options (monetary policy has reached its limits) but unwilling to admit defeat on its target of 2% inflation, the BoJ is considering the most extreme action. Market speculation that Japan is considering helicopter money increased as former Federal Reserve Chairman and helicopter advocate Ben Bernanke met privately with BoJ Governor Haruhiko Kuroda in Tokyo. Yet, even if the BoJ does not conduct what is generally referred to as "helicopter money" continued monetary and fiscal stimulus will have basically the same effect.

Analysis & Portfolio - Swissquote Bank Strategy Desk





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.