SWISSQUOTE

WEEKLY MARKET OUTLOOK

8 - 14 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

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Economics

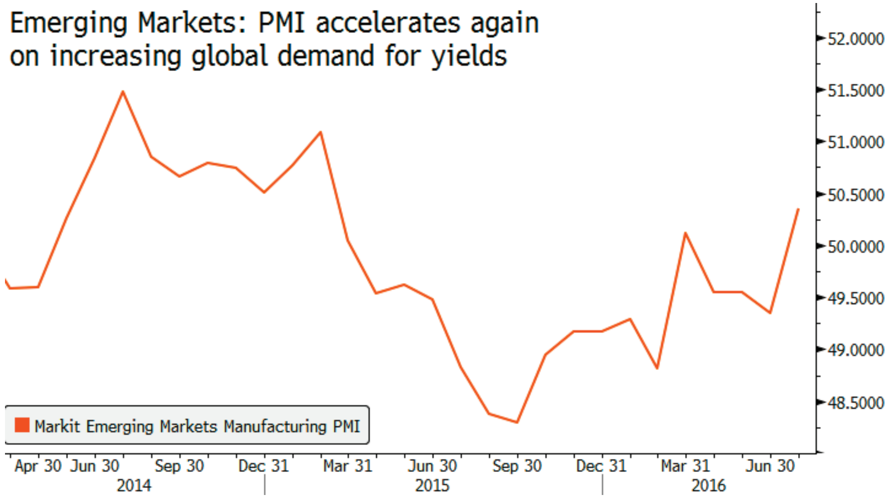
EM Momentum Should Continue

The last two weeks activity by global central banks and reaction by financial markets has played directly into our over-arching theory for asset pricing. Simply stated central banks loose, unorthodox monetary policy has placed a continuous "put" under risk-appetite. A "put" that cannot be shaken by weak fundamentals, geopolitical worries or threat to world's largest economic union. Equity volatility continues to contract while corrections in risky assets are getting smaller. The BoE's aggressive stance including 25bp interest rate cut to a record 0.25%, £70bn expansion of QE including £10bn corporate bond buying, and Term Funding Scheme, sounds nice on paper but hardly addresses the structural, Brexit created issues (BoE own projections significantly downgrade growth).

The clearly stated stop-gap action was celebrated by global financial markets by driving equity indices higher, despite zero concern over liquidity or unsatisfied loan demand. Value driven asset manager might attempt to argue that fundamentals still matter, the fact is they don't. The out-performance of EM currency problem nations, BRL, ZAR, RUB and recovery of TRY highlights this point.

The current macro-environment should continue to support dominate yield-seeking carry trade. With volatility subdued, G10 yields nearly non-existent (making EM yields appealing) and steady improvement in economic activity (although merely a rationalization to take extra risk) demand for EM looks to last the summer. The sharp reversal in oil prices while raw commodity prices such as copper and nickel reflecting progress in EM manufacturing PMIs has held ground makes us constructive on Asia EM currency and fixed income.

In addition, China has begun to shirt towards more stimulus in further reduction to RRR, as data indicated that export slowed 3.5% and inflation moderately to 1.8% in July, which should give regional demand a kick. The primary risk to this call would come from the Fed and a premature September interest rate hike. However, we view any decision to be data dependent up into the Yellen's Jackson Hole symposium and September meeting, and unlikely to happen.



Economics

RBNZ's Cut To Weigh On The Kiwi

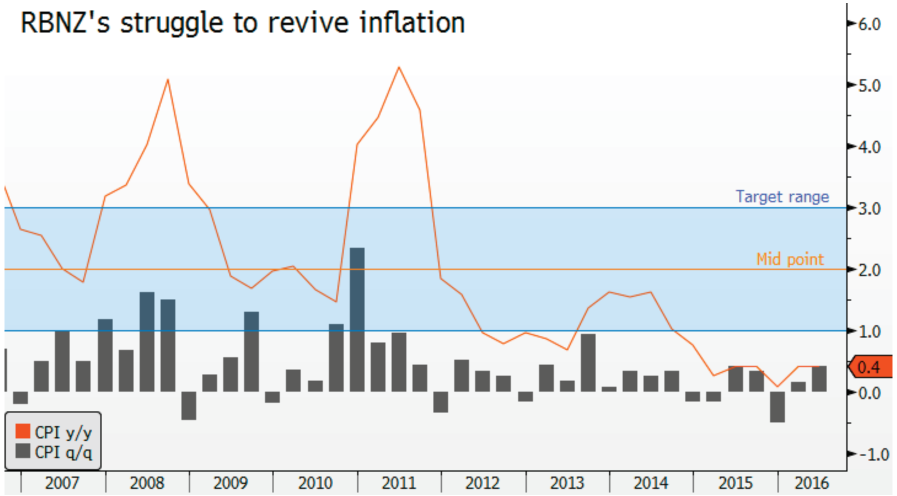
In spite of the absence of economic data from New Zealand, the Kiwi held ground against the US dollar last week. The chase for higher yields coupled with fading expectations for a Fed rate hike in 2016 prevented the Kiwi to lose ground. However, the risk in NZD/USD is clearly to the downside as the RBNZ is expected to cut the official cash rate by 25bps to 2% at its next meeting on August 10th.

Indeed the central bank may be poised to cut rate on the heel of a disappointing second quarter inflation report. Headline CPI dropped unexpectedly in the second quarter, sliding to 0.4% on both a quarterly and yearly basis, missing projections for both the market and the RBNZ. The market was expecting a read of 0.5%y/y, while the central bank forecasted CPI to rise 0.6%y/y during the June quarter. Tradable inflation (i.e. domestic inflation) fell 1.5%y/y, reflecting the unexpected rise of the Kiwi over the last few months, while non-tradable inflation increased 1.8% y/y as housing market prices continued to gain momentum.

In addition, a couple of weeks ago the Reserve Bank of New Zealand released an economic update. The statement was very dovish and clearly set the stage for a rate cut in August. The RBNZ highlighted the diminished prospect for growth in spite of a very stimulatory monetary policy, the "fragility of global financial markets" and persistent uncertainties about the outlook. Most importantly, the central bank appeared to be quite unhappy with regards to the strength of the Kiwi as the trade-weighted exchange rate was 6% higher than assumed in the June statement.

As a consequence, we expect the RBNZ to cut the official cash rate by another 25bps at its August meeting, which would bring the OCR down to 2%, in spite of the negative effects it would have on the housing market. Indeed housing prices have been fuelled by the low price environment and another rate cut would definitely increase the upside pressure on these prices. However, the Reserve Bank had clearly indicated its intention to take separate measures to stem the housing bubble by using lending restrictions and tightening the LVR.

On the technical side, the NZD/USD resumed its rally on Friday and brokethe 0.7182 resistance implied by the 61.8% Fibonacci line (on July's debasement) and is now heading toward the 0.7257 resistance (high from August 2nd). Given the strong likelihood of a rate cut, the pair will most likely return quickly towards 0.6950, especially if the RBNZ release a dovish statement to emphasize the central bank's easing bias.



Economics

Good Jobs Report Won't Be Sufficient For A US Rate Hike

Is ADP a good indicator of the NFPs?

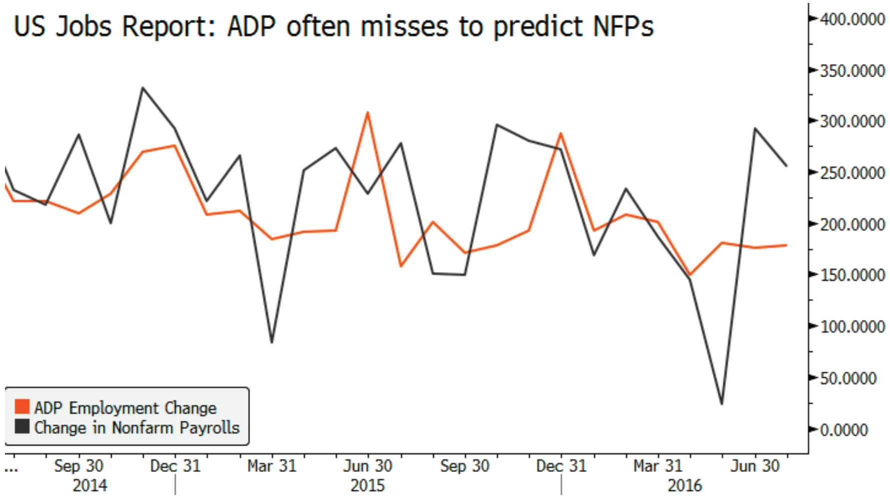
Several times, ADP data has failed to accurately predict NFPs. In May, the difference was spectacular, with ADP predicting 173k new jobs, while the NFP payrolls only printed at 38k. June data also reported a strong difference but was more positive for market sentiment. ADP predicted a 172k increase and NFP reported 287k jobs creation. It is nonetheless important to say that with both jobs data indicators providing different figures it is confusing to determine a clear trend. NFPs are largely more volatile, while the ADP has been relatively steady and when it comes to predicting the outcome of NFPs, the ADP has missed the mark for the last two releases.

At last it seems as though the market is content so long as both indicators are strong. This is what happened, July ADP came in at 179k beating expectations by 9k and NFPs recorded a great 255k, 65k more than the consensus.

What to expect after the NFPs?

A week after the FOMC, the market is still scrutinising every morsel of information for hints that monetary policy will be tightened. Markets are still assessing a 37.3% probability of a rate increase for this year. We maintain our position that the Fed is dovish and not ready to take further action that would weigh on the American economy.

Fifth of August's NFPs will be no different. The US election will provide the Fed with its next excuse for not raising rates. Tightening monetary policy is way more than just having strong jobs data and an inflation that is headed towards the target. The reality is that 15% of the US population is on food stamps which represent nearly 50 million Americans. The Fed wants to appear hawkish but is actually dovish. Currency-wise, we maintain our long-term view that the dollar should continue dropping on the back of continued failed expectations that a rate hike will happen. The slight decline of the EUR/USD amid the jobs data is a great entry point to reload long positions.



Economics

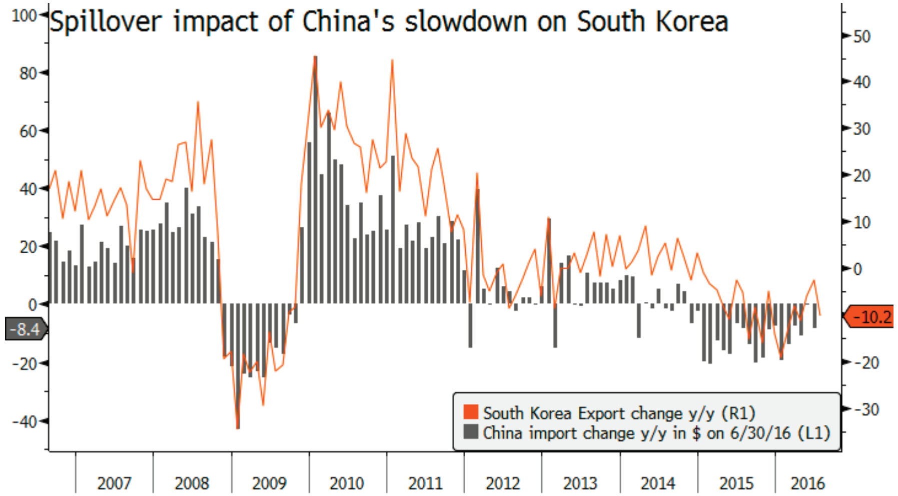
South Korea: Rate Cut Still In The Pipeline

Since the beginning of the year, the South Korean won has been rallying strongly against the US dollar as investors continue to chase higher yields in a low rate environment. The South Korean economy outperformed most of its peers in the second quarter as it grew at a solid pace of 3.2%y/y (versus 3.0% expected), while the unemployment rate fell to 3.6% in June from 3.7% in the previous month. Therefore, the BoK held fire at its July meeting as it kept its repo rate of 1.25% on hold after slashing 25bps in June.

At first glance, the picture looks fine but the country's outlook is not that bright as exports fell another 10.2%y/y in July compared to -2.7% in June and -6.7% median forecast. Imports contracted 14%y/y (verses -10.5% exp. and -8% previous). Consequently, the trade surplus slid to $7.8bn versus $8.2bn median forecast and $11.5bn in June.

Overall, the data suggests that the recent appreciation of the won has dampened further the country's exports amid the Chinese slowdown. The minutes of the July's BoK meeting indicated that the MPS is waiting for further indication regarding the effects of the previous rate cut before cutting rates again. However, since central banks across the planet continue to ease their monetary policy further and since the Fed is expected to remain on the sidelines for a while yet, the BoK may have no choice but to join the currency battle and cut its repo rate in order to prevent the KRW from appreciating. In addition, the inflation data released last week showed that price pressure remained subdued and that CPI is still struggling to move towards the 2% target. Headline CPI printed at 1.6%y/y, missing consensus of 1.7%.

USD/KRW is trading at a 19-month low as it hit 1,106.37 on Tuesday morning. On the downside, a support lies at 1,097.47 (low from June 22nd), while on the upside a resistance can be found at around 1,200.



FX Markets

IMM Non-Commercial Positioning

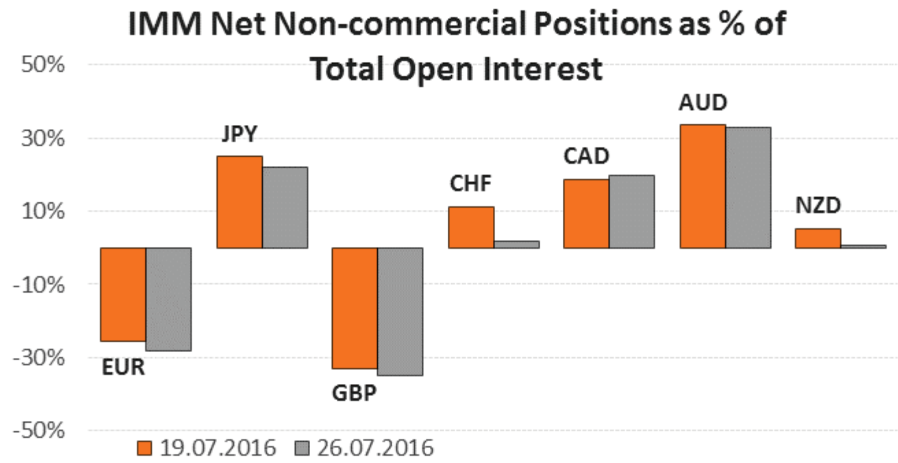
The International Monetary Market (IMM) non-commercial positioning is used to visualise the flow of funds from one currency to another. It is usually viewed as a contrarian indicator when it reaches an extreme in positioning.

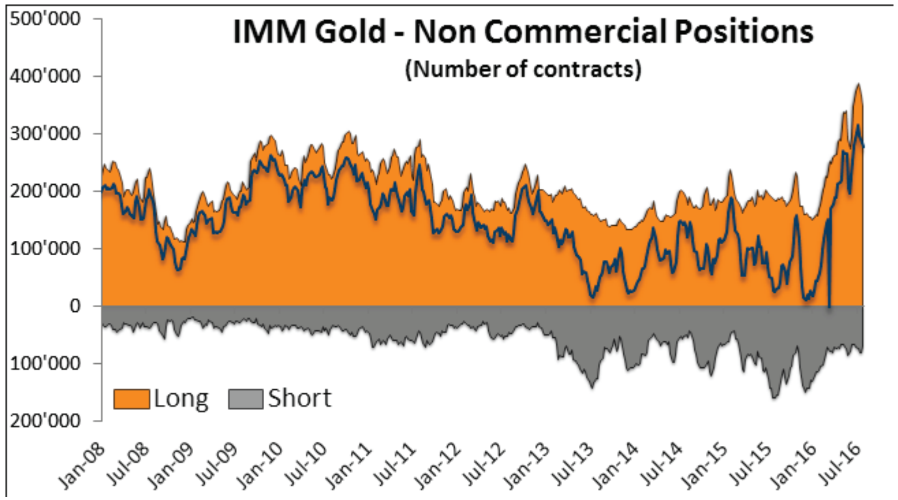
The IMM data covers investors' positions for the week ending July 26th 2016.

The BoE cut rates to 0.25% as widely expected by financial markets. Net position is still largely short and investors are betting on a more difficult situation for the UK. The consequences of the Brexit vote still have to be assessed. The GBP short position is at a record high.

The EUR net position is also shorter. Uncertainties are growing. Most of the central banks in the world are largely all-in and the efficiency of the monetary policies is more questioned. On top of that, the future of the EU appears darker.

Safe haven bets are being reduced. Yet, speculators are still long CHF and JPY. Commodity currencies seem to be the new place to be with CAD and AUD largely long which demonstrates that global uncertainties are too important. The risk-off sentiment drives investor towards Gold.





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