SWISSQUOTE

WEEKLY MARKET OUTLOOK

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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

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WEEKLY MARKET OUTLOOK - An Overview

Economics

Fade The Trade Escalation Hype

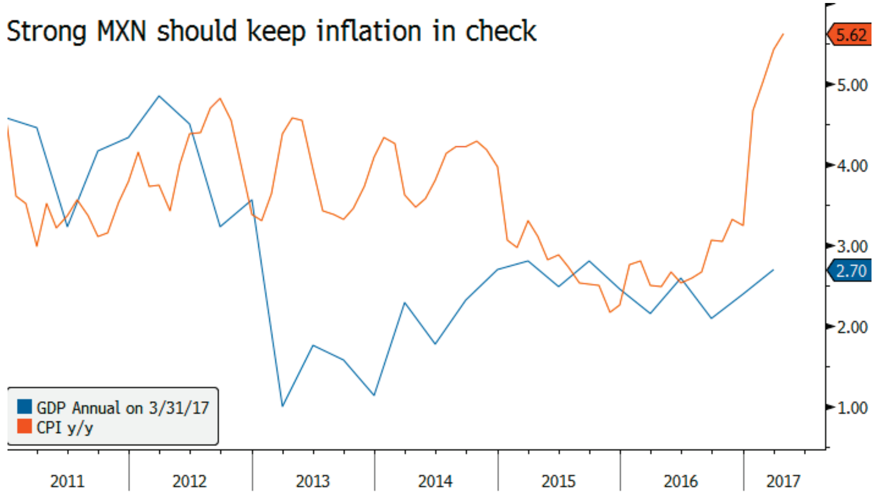
We have seen President Trump fire up the extreme populist platform of protectionism in an attempt, in our view, to score some quick points as his first 100 days milestone approaches. First Trump slapped Canada with up to a 20% tariff on lumber imports, then he forced Canada and Mexico to agree to renegotiate NAFTA. He closed the week threatening to “terminate” Korus, the US - S.Korea trade deal (potentially a tactic to get S. Korea to pay for THAAD). Traders were quick to sell the underlying currencies CAD, MXN and KRW on the escalations in trade tensions. However, as with much of Trump’s actions, we suspect that recent moves will be short-lived as real underlying policy initiatives are unlikely.

In the case of Mexico, events in Venezuela should provide a stark warning to the potential effect of destabilizing measures. The Trump administration is unlikely to push Mexico too hard, opting to have a safe, friendly cushion between the US and South America. MXN has had a difficult time with weaker oil & copper prices and rumours that President Trump has ordered a draft letter to leave NAFTA. The news injected some volatility into MXN as the currency came under significant selling pressure against the USD. Yet, Trump’s sudden reversal from withdrawing from NAFTA to renegotiation should be MXN positive. From a fundamental standpoint 1Q annual GDP rose 2.7% above prior read of 2.4% (2.5% exp) indicating steady expansion. While Banxico hiking cycle come to an end as inflation and exchange rate collapse has been managed.

The partial unwinding of the extreme risks of protectionism will lower concerns that Emerging Markets currencies are heading towards a correction. The MSCI Emerging Market Currency Index is trading just below its two-year high.

From a macro perspective, the affirmations that the ECB and BoJ will maintain their accommodating policy for the foreseeable future indicates that risk-taking and yields-seeking behaviour should resume.

Given our current view on global conditions, we anticipate MXN will recover lost ground. We anticipate that USDMXN, despite is slightly oversold positioning, will retest 18.50 lows.



Economics

US Budget Deficit Back Under The Spotlight

Last week, financial markets continued to digest the result of the first round of the French election but the focus is slowly shifting towards the US as President Trump made some announcement about his “phenomenal” tax reform and also put his protectionist trade policy back to the drawing board. Indeed, the market is slowly shifting focus from the French election and I currently pricing a Macron victory at the second round, which helped to restore market’s confidence and gave a boost to European equities and the EUR.

During the previous week, the dollar index was mostly trading sideways, suggesting that the market is very suspicious regarding Trump’s announcement. In fact, it seems that it is not even buying his stories anymore and would rather wait for concrete actions.

We are very suspicious that Trump’s tax cut reform will pass through Congress as it will make the US deficit balloon. In addition, the timing couldn’t be worse as the US budget deficit has become the new hot topic recently as the US government is running out of money, meaning a government shutdown is looming. There is little chance that the Trump administration will get Congress to sign its tax cut reform, while at the same time getting it to sign off another spending bill. Trump is indeed in a deadlock, without passing a reform aiming at balancing the drop in tax receipts, it seems complicated to pass the tax cut bill.

In such an environment, we should continue to see some inflow in the single currency. The shift towards riskier assets should continue, even though the market is converging towards a new port-French-first-round-election equilibrium for now. Against this backdrop, we would rather avoid taking long USD positons, except against the JPY, waiting for further clarity on the US outlook and more specifically the US budget story and the tax cut plan.

Politics & Economics

ECB Relieved After First Phase Of French Election

Financial markets feared a second round between Jean-Luc Mélenchon and Marine Le Pen who was likely to trigger some volatility. Marine Le Pen's final result below 22% is disappointing as she was expected in various polls to reach between 27% and 30%.

The failure of Le Pen or Mélenchon to sway undecided voters or unlock closely-guarded voting behaviours will come as a major relief to investors fearing uncertainty over whether the second round would bring a new set of complexities. At present, extreme volatility has been avoided. Emmanuel Macron and Le Pen will move forward to the second round run-off on May 7.

The result is very market-friendly. The failure of Marine Le Pen or Jean-Luc Mélenchon to surge on voting day should be viewed as a vote for the EU. Eventually, Emmanuel Macron is now very likely to become the new French president. Most of the runner-up such as François Fillon who scored around 19%, are calling for a Macron vote for the final vote in two weeks. Even Mélenchon, which program was very similar to Marine Le Pen's has been calling, through his lieutenants, to vote for Emmanuel Macron.

There had not been a massive relief, if any, in financial markets. However the single currency appreciated slightly against the swiss franc. There's nonetheless no fear for the second round. Final results estimates are calling for a 60% Macron's victory. European Union seems to win a battle and attention should carefully shift towards the German's election in August.

We anticipated no extreme volatility in the FX market, with marginal Euro buying (as markets had positioned for this outcome) as exit polls become official results. We remain long EURCHF on a rejection of an anti-EU vote.

Draghi showed optimism on Eurozone economy

Last Thursday, European Central Bank meeting was in the middle of the French Presidential election and the European institution certainly welcomed Emmanuel Macron's victory in the first round as there were certainly fears of a second round pitting Jean-Luc Mélenchon against Marine Le Pen.

This meeting was very useful to the extent that Mario Draghi was optimistic in regards to a future tightening even though the current level of asset purchases (€60 billion) will continue until year-end. We believe that for some more time, the ECB will remain committed to low rates.

Markets are likely to price in better confidence and we remain bullish on the Euro in the short-term. In Europe, economic fundamentals are better, inflation is picking up and unemployment has decreased, even though it remains very high in peripheral countries. Financial markets are clearly not pricing anything else but a Macron victory in France, which seems to rule out any political risks for the ECB.

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