WEEKLY MARKET OUTLOOK

14 - 20 August 2017

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WEEKLY MARKET OUTLOOK - An Overview

Economics

NZD Tumbles As Economic Outlook Weakens

Among the G10 complex, the New Zealand dollar was the worst performer last week, falling the most against safe haven currencies such as the Japanese yen and the Swiss franc - down 3.10% and 2.85%, respectively. The rapid collapse of the Kiwi is due to the accumulation of disappointing economic data together with the unwinding of large speculative positions and a somewhat renewed interest in the US dollar that was triggered by an encouraging NFP report.

On the data front, the last RBNZ's survey showed that one-year inflation expectations slid to 1.77%y/y from 1.92% three months ago, while two-year ahead inflation expectations fell to 2.09%, down from 2.17% previous reading. This setback came on the back of a worse-than-expected second quarter jobs report that highlighted the anaemic employment growth and poor wages pressure.

Last but not least, at the occasion if its latest monetary policy meeting, the Reserve Bank of New Zealand made a dramatic shift in its language as it made clear it is not happy, at all, with the current strength of the Kiwi. Assistant Governor McDermott suggested for a second that the bank could move back to intervention should the circumstances require so. However, he added as he tried to allay an overreaction of markets that it was just a little nudge, rather than “a slap across the face”.

After topping $0.7558 on July 27th, NZD/USD has returned at around 0.7275 (Fibonacci 50% on May-July rally) and has been sitting there since Thursday as investors kept wondering whether further weakness is reasonable. In the short-term, the continuous flow of lacklustre data from the US will probably spur investors to maintain their negative USD bias, which should prevent the Kiwie to depreciate further.

In the medium-term, this is a different however as the Federal Reserve is expected to go a step further towards tightening. Even a baby step could ignite a dollar rally.

Economics

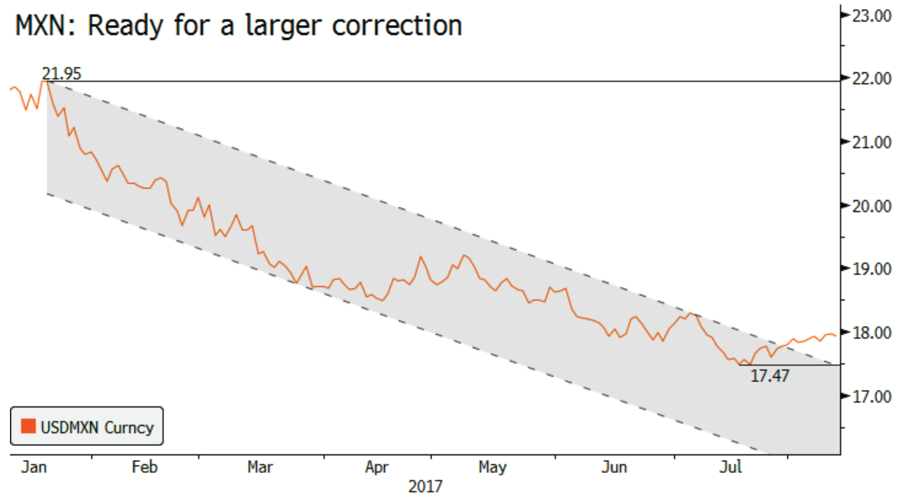
Banxico Is Opting For Caution On Monetary Policy

It was widely expected by financial markets that Banxico would maintain, earlier last week, its rate differential with the Fed. The Mexican central bank keeps trying to avoid capital outflow that would result from a narrower rate differential. As a result Banxico decided to hold its overnight rate to 7%. We remember that Banxico changed in 2015 the agenda of its meeting to carefully follow Fed meetings.

This year the central bank has increased four times its overnight rate triggering the strengthening of the MXN. But now, we see things are slowing down. When looking towards the Fed, we believe the US private institution will have more difficulties to deliver further rate hike before 2018 and that the promised shrinking of the balance sheet could provoke further turmoil. This is why we see Banxico cooling down its aggressive hawkish monetary policy and lower its interest rates before year-end.

However, Banxico has definitely some time to do it. Indeed, for example Mexican exports have largely increased in 2017 despite the MXN strengthening which went from 22MXN to almost 17MXN in 7 months against the greenback. This is mostly due to the oil prices jump this year but also to the uncertainties regarding the free trade agreement between US and Mexico that should be renegotiated - Trump estimates that the deal favours low-wage countries.

Other than that, the fundamentals of Mexico are still on the soft side and renewed lower oil prices could very easily reveal all underlying difficulties of the countries. We are turning bearish on the MXN as we believe that Banxico will likely not let the currency appreciate forever knowing that the US giant recovery may take some more time.



Economics

USD Rally Delayed Amid Weak Data

Despite a consolidation in the US dollar last week, the greenback has been unable to reverse for good the negative trend. Yet the July jobs report, which was released the previous Friday, seemed to have marked a turning point. But it was without counting on a few Fed members who talked down the dollar and the release of - once again - disappointing data from the world's largest economy.

The dovish comments from two Fed members were one among several factors that prevented the dollar to recover firmly. Both Bullard and Kashkari emphasized that the weak inflationary pressures were still a problem and added that it cannot be solved by an improving job market. St. Louis Fed President Bullard declared that "the current level of the policy rate is likely to remain appropriate over the near term," and added that the weak inflation reading were concerning because it suggests this setback is not due to temporary factors.

Finally, the July inflation report released on Friday did not allow for excess optimism. Indeed, once again, the data came in on the soft side. Headline CPI printed at 1.7%y/y, while the market was expecting a reading of 1.8%. The core gauge, which excludes the most volatile components, held steady at 1.7%, matching expectation. The report a not a game changer as the weakening inflation pressures is no secret. Unfortunately, this is again a warning bell which is calling the Fed to take it easy with tightening. According to the last hard data from the US economy, there is no reason to expect a sustained dollar in the short-term.

For some time we have been defending the idea that the dollar's debasement was coming to an end, arguing that this moment has been approaching fast. This assessment is not fundamentally altered as the Federal Reserve is the best placed amonf central banks to tighten monetary conditions. However, faltering economic data doesn't allow for excess optimism. We are therefore forced to adjust our assessment, especially the timing of a potential dollar recovery. We still advocate that such a recovery is underway but we may have to wait until the last moment, most likely the end of the month, just before the Fed meeting, to start building long USD position.

Title	Gold & Metal Miners

The sudden collapse in commodity prices in 2014 sent mining stocks into free fall. In the long term, however, precious metals - and gold in particular - are the perennial go-to sources of protection against inflation and economic downturns, something investors should be looking out for. The gold market is dynamic, and there are compelling reasons why gold producers could rally. Consumer demand remains solid, with around 2,500 tons of gold mined worldwide every year. Over the long haul, gold as a commodity has appreciated by more than 287% over the past 15 years; by comparison, the S&P 500 has gained less than 44% over the same period. In a period of central bank policy shifts, it is reasonable to envisage a rebound in metal prices - something mining stocks will benefit from. Gold miners are a good way to tap into the benefits of precious metals without paying storage costs.

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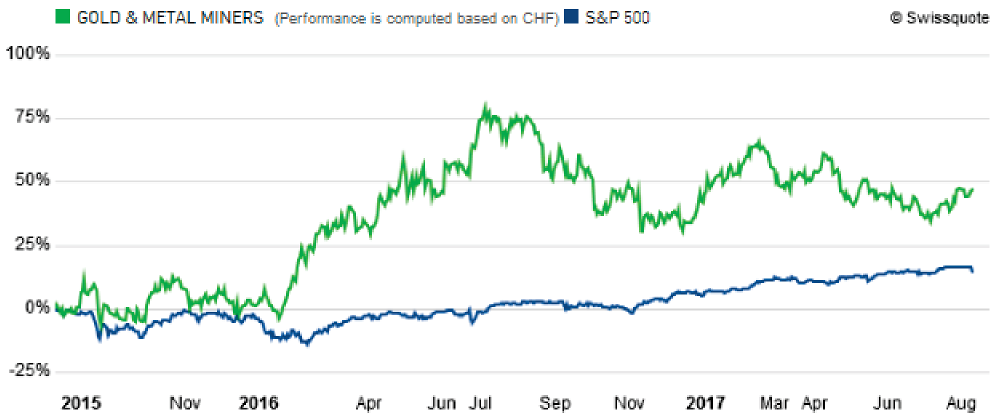

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