WEEKLY MARKET OUTLOOK

12 - 18 February 2018

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WEEKLY MARKET OUTLOOK - An Overview

Economics

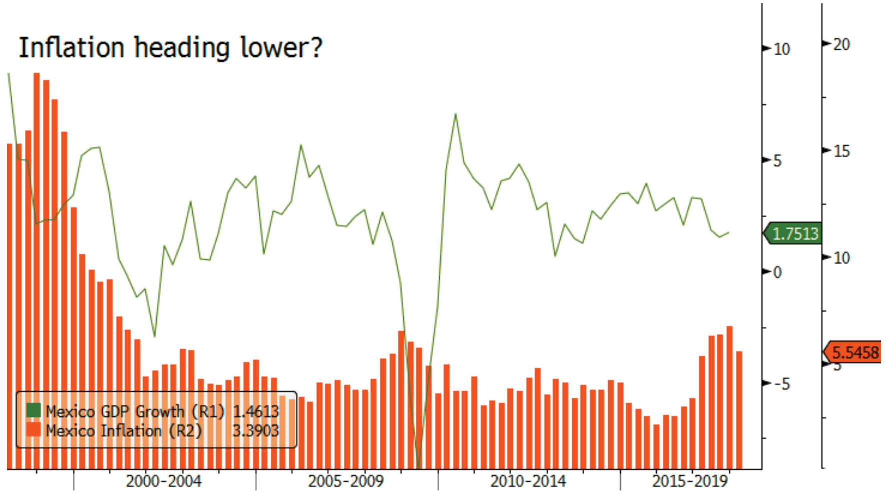
Mexico Peso Looks Interesting

While resurgent volatility suggests that risky asset are still in jeopardy, in general, high beta FX have not been materially affected. S&P 500 saw all sectors close down, part of the global stock collapse, US yields rallied and volatility surges yet FX remained stable. This lack of contagion to us indicates that we are seeing a technical correction rather than a structural shift. Unlikely that rise on volatility will derail the broader positive outlook. In the FX Mexican peso is increase becoming attractive, as MXN has been the most responsive currency during periods of stress yet remarkably stable currently.

Last week Banxico raised policy interest rate 25bp while providing a hawkish tone signalling more hikes are likely. The Mexican central bank is increasingly unconvinced about inflation outlook. The interest rate hike in December, was followed by a February rate rise as expected. In its communication, Banixco highlighted risks to inflation and now expects the 3% target in 2019. It's unlikely given domestic and global environment that inflation will come down meaningfully. GDP had contracted in Q3 due to natural disaster, 4Q recorded solid growth (probably in part catch-up effects).

We don't see any dovish policy communication until 2019 and could see rates peak at 5.75%. Risk of the NAFTA renegotiations and the presidential elections due on 1 July have weighted on business and consumer sentiment. We continue to see a soft NAFTA result. The sixth round of negotiations took place in January where US, Canada and Mexico stated that progress had been made. Despite Trumps feet stomping US - Mexico trade economy is deeply integrated. Any protectionist action would have complex result and most barriers can be easily circumvented.

While peso faces volatile times wee would see current USDMXN strength as an opportunity to reload shorts.



Economics

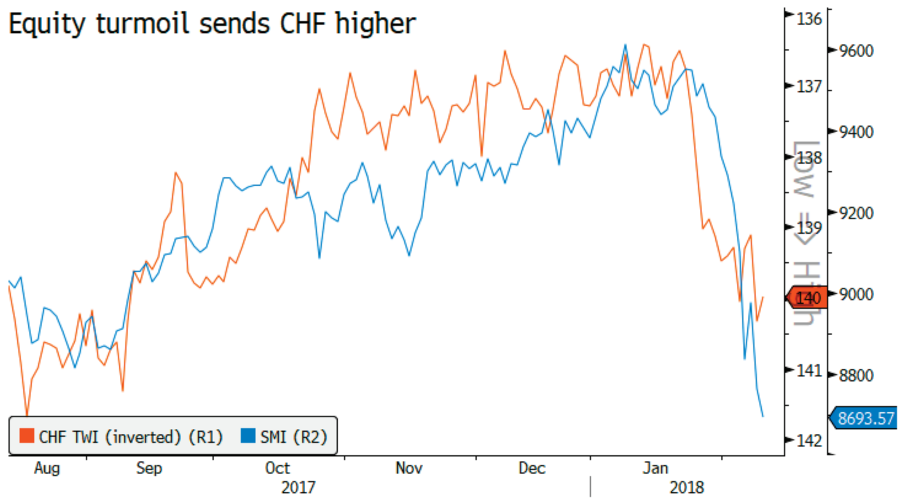
EUR/CHF Falls To 4-month Low Amid Equity Rout

The FX market has been only slightly affected by the sell-off in equities. Even safe-haven currency were of limited interest to investors. EUR/CHF spent most of the week trading sideways at around 1.1550 before sliding to 1.1447 on Thursday as the equity market sell-off resumed. However, the currency pair went through a choppy session on Monday as the implosion several complex exchange-traded notes started to spill over into the stock market.

On the economic side, the latest batch of hard data had also little effect on the pair. The unemployment rate held steady at 3.3% in January (versus 3.4% expected), while the seasonally adjusted measure stagnated at 3.0%. January inflation measure are due for release Monday morning at GMT 8:15. The headline measure is expected to come in at 0.8% on a year-over-year basis, while the gauge should have contracted 0.2% compared to December last year. Overall, the inflation will go unnoticed, as the market's attention will remain on equities and VIX.

Given the recent appreciation of the Swiss franc – the CHF appreciated almost 3% against the single currency from its high from mid-January – it will be interesting to see how the Swiss National Bank reacted to this appreciation. Total sight deposit held at the SNB increased slightly during the first two weeks of January (+3.03 billion) but are still below the all-time high of August 2017.

Since the financial crisis, the publication of Swiss data always had little impact on CHF crosses, especially EUR/CHF. Given the turmoil in financial markets, the release of the data will mostly go unnoticed. Market participants will continue to monitor closely developments in the equity market and more specifically the VIX index. Against such a backdrop, we suspect that the bias is on the downside in EUR/CHF, as a worsening of the risk sentiment remains a live possibility.



Economics

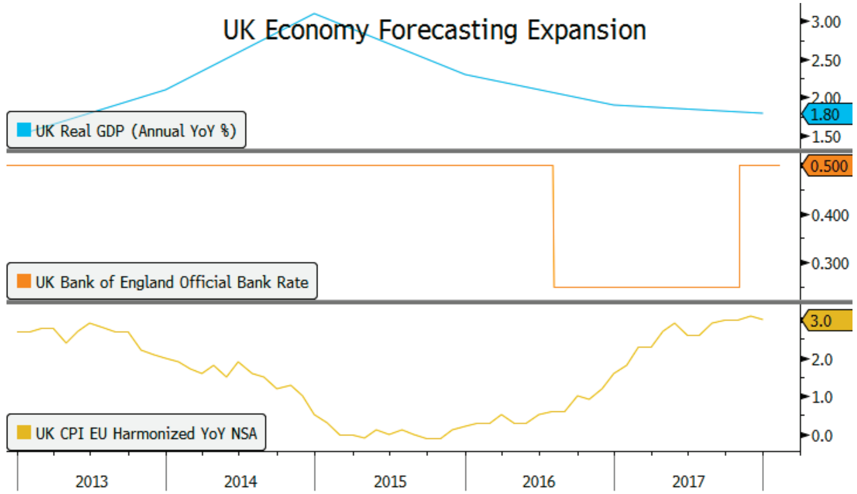
UK Growth Forces BoE To Bring Nearer Rate Hike

Since the beginning of the year, the United Kingdom confirms durable growth numbers and doesn't seem that much bothered by pending Brexit negotiations that are most likely to last up to 2021 instead of 2020, as painful free-trade agreements still straggle. UK December 2017 GDP Y/Y reached 1.80%, slightly below 2016 data presented at 1.90% and expected to stabilize in January 2018 in Y/Y basis.

Based on February inflation report, the UK economy starts growing at a more vigorous pace and inflation is expected to reduce as today's BoE Interest Rate is maintained at 0.50%, same level since November 2nd 2017. Speculations of a rate hike in May 2018 are increasing as the Monetary Policy Committee confirmed a more optimistic view of economic growth and that it intends to increase interest rates faster than previously anticipated, increasing estimated probabilities of May 5th 2018 BoE meeting to raise interest rates of 25 bps by up to 70%.

Accordingly, 10-y Treasury Bonds started increasing by 6.25% at 1.65. The announcement also impacted equities forcefully, decreasing FTSE100 and FTSE250 of -0.83% and -1.06% respectively while GBP/USD and GBP/EUR pairs strengthened by +1.03% and +1.09% at 1.40 and 1.14. At-the-money 3-months put/call option prices implied volatility decreased by -0.67%.

In our view, the UK economy is signaling strong economic stimulus, boosted by continuing exchange pass-through advantage induced by June 2016 Brexit Referendum outcome and constructive Brexit negotiations. In this backdrop, we see no further setback to a BoE interest rate of 0.75% in May 2018, as an inflation target of 2% is considered whereas December 2017 inflation rate remains at 3%.



Themes Trading — Swiss Smart Beta

Switzerland's stability has provided ideal soil for global brands to develop. Swiss stocks have a reputation of being high quality and tend to provide stable returns during times of geopolitical uncertainty. With President Trump, Brexit, European elections and global protectionism, the world has become significantly more unpredictable. This portfolio sources high-dividend Swiss stocks and provides an active quantitative overlay to optimize risk/reward potential.

The Swiss Smart Beta theme consists exclusively of stocks from the Swiss Performance Index (SPI). The selection process identifies stocks with a high dividend yield and a market capitalization in excess of CHF 100 million. Illiquid stocks are screened for constant bid-ask spread and daily average dollar volume traded. To enhance risk diversification, the portfolio is weighted using an equally-weighted risk contribution approach. In summary, this means the allocation is calculated in such a way that each stock contributes on an equal basis to the total risk of the portfolio. This approach allows for low volatility and, in so doing, increases the risk/reward ratio.

Swiss Smart Beta Certificate is available for trading at :

https://www.swissquote.ch/url/investment-ideas/themes-trading

Since inception	▲ 16.46%
1-month return	-2.09%
Return day	0.00%
Est. dividend yield	4.24%
Inception date	01/09/16

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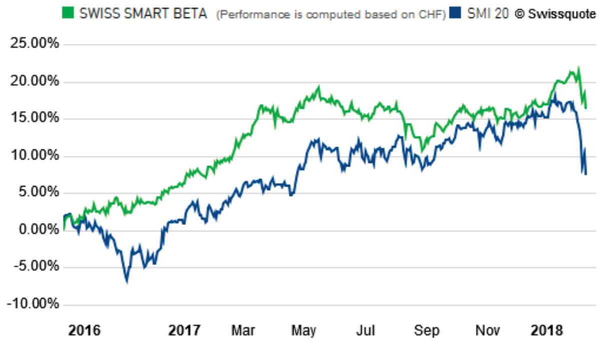

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