SWISSQUOTE

WEEKLY MARKET OUTLOOK

19-25 February 2018

DISCLAIMER & DISCLOSURES

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WEEKLY MARKET OUTLOOK - An Overview

Economics

Dont Sell Europe Yet.

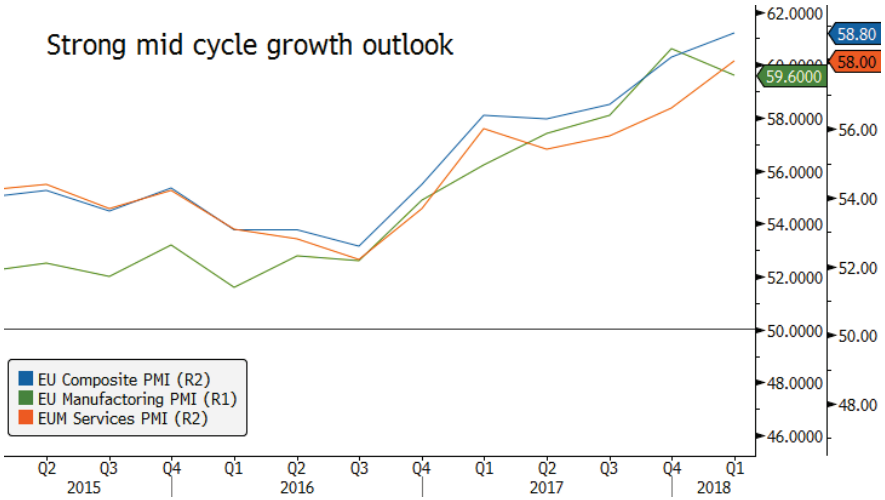
Bloomberg's article on Bridgewater Associates $18bn short on Europe highlights a growing shift in markets optimistic outlook on the Eurozone. In the view of European skeptics, the recent financial market turmoil will dent investor's sentiment and in turn spoil over into household and business confidence. We are suspect, the clearly volatility triggered sell-off, lacks fundamental basis needed for a sustained correction. Both the Feds policy strategy and consequential rise in US yields has been well telegraphed, unlikely to catch anyone by surprise. Even higher inflation reads, unless going parabolic, is unlikely to surprise traders. We believe the era of innocence is over were traders will become more cautious but doesn't necessary mean the end to historic bull-run.

Economic data across Europe remains supportive. Should we get a marginal weakness in February PMI reads the current elevated levels would easily offset seasonal weakness. Loose financial conditions continued to outweigh negative effects of a stronger Euro. The EU had a trade surplus with the U.S. of €120.8bn in 2017, up from €113.1bn 2016, according to Eurostat. Exports from the EU to the U.S. increased to €375bn in 2017 from €363.5bn prior, while US imports increased to €254.2bn from €250.4bn. Elsewhere, healthy consumer caused domestic car market sales to surge 6.8% in January, reaching a new 10 year high as the region's economy accelerated.

The primary risk to the current outlook is not the Fed or March 4th Italian elections but the risk the ECB will signal earlier than expected tighter policy. Yet, we suspect this is a low probability event. First underlying trajectory of inflation remains weak. We only imagine the first minor hike in the depo rate in late 2018, by 10bp to a level of -0.3%. ECB's Nowotny, made it clear it will be while before the ECB key interest rate increase. The ECB's asset purchases will last until September.

"discuss whether or not to end it. I make no secret of the fact that I don't think we will need it, at least not in its current form. And only after we have ended it will the question of interest rates come into play." Very clear in our view.

EUR continues to advance against the USD as higher bond yield fail to attracted investors interest. The key driver of dollar selling is due to synchronized global economic expansion, as capital is leaving the USA search of opportunities. With globalization of investment, hitting a new peak a few basis points in the US will not stop the exodus.



Economics

Is the USD sell-off over?

It was another bumpy week in financial markets as the US economic situation keeps investors on their toes. Indeed, the market remains observant for any signs of change in the US that could impact the pace of rate tightening by the Federal Reserve. Last Wednesday was a concrete example as January inflation hit the street.

Both inflation gauges increased more than median forecast. The headline measure printed at 2.1%y/y, compared to 1.9%y/y consensus, while the core measure came in at 1.8%y/y versus 1.7% expected. The steady appreciation of energy prices explains most of the upside surprise in the headline CPI. Regarding the core measure, the broad-based USD weakness of the last couple of months is undoubtedly the main reason behind this stronger Core CPI read.

Initially, financial markets reacted violently to the release as the upside surprise could be the trigger for the Fed move towards to a more aggressive path of tightening to tame accelerating inflation pressures. European equities and US futures moved in negative territory with the Dow Jones losing instantaneously 2%, while the Eurostoxx 50 fell 1.4%. In the bonds market, the entire US yield curve shifted to the upside. The VIX index jumped to 25.7 and the greenback strengthened.

However, it didn't take long before investors start shifting attention towards retail sales figure and realise that consumer didn't spent much in January. Advanced retail sales contracted 0.3%m/m (versus +0.2% median forecast), when excluding auto & gas the contraction is trimmed to -0.2%. Given the sharp and steady increase in consumer spending since September last year, this decrease is in consumption is rather due to the fact that US people are taking a temporary break after the Christmas season, rather than the sign of persistent weakness in the economy.

Indeed, the unemployment rate is very low and wage have finally started to grow. There is therefore nothing that suggest this would last through the first quarter.

Therefore, investors quickly started to dump the greenback again and bought stocks as their concerns about accelerating inflation pressure have been alleviated. On Friday, nothing has changed: the greenback was sold-off, with the dollar index hitting its lowest level since December 2014 at 88.25, while equities across the globe continued to recover.

The greenback is not out of the wood yet as investors are paying more and more attention to the current account and fiscal deficit of the world largest economy. Indeed, the US will have to find fresh money and with rising interest rates and the Fed unwinding its massive bond position, the burden could only be heavier for the country. The trend seems here to stay, meaning that further USD weakness should be expected.

Economics

Japan to maintain monetary policy loos for the time being.

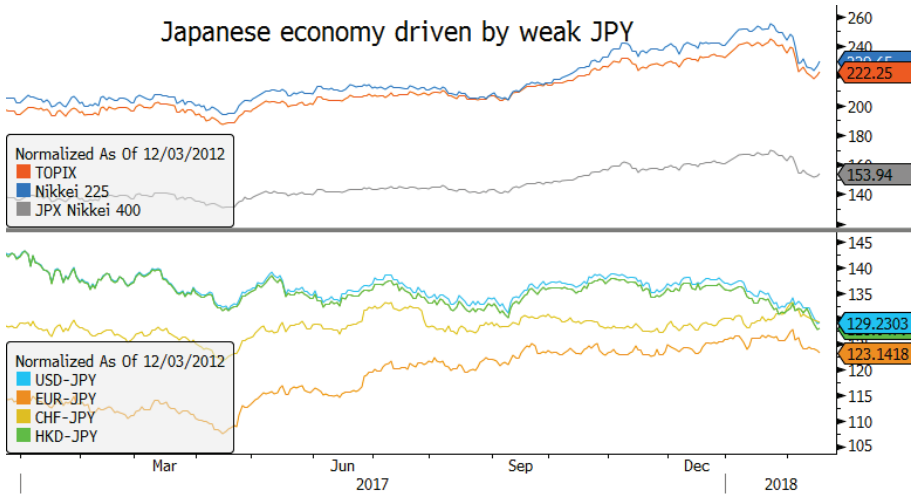
Japanese Prime Minister Shinzo Abe confirmed on Friday his decision to maintain Haruhiko Kuroda as Bank of Japan's leader for the next five years to come, as expected. This decision provides a clear signs of intent to maintain monetary stimulus at current level, all this in the context of a rather weak 4Q 2017 GDP growth, published on Wednesday 14th 2018 at 0.10% (consensus: 0.20% - previous: 0.60%; December 2017 GDP Y/Y:1.50% - previous: 1.90%), lowest rate since December 2015, suggesting that Japanese economy has still a long way to go until it reaches its GDP growth target of 2.0% for 2018.

Supported for the last 18 months by a weak JPY that allowed the Japanese economy to focus on its exporting industries in order to expand gains locally, we see further increase in JPY against major currencies as a serious threat. China and the US being the biggest investors of Japanese goods and services on trade weighted value (China: 31.20%, USA: 20.81%), we see current exports increase on Y/Y basis published at 4.50% (previous: 4.0%) as rather high and are expecting them to reduce strongly for the periods to come if the JPY continues its progression, adding further headwinds to foreign sales.

Recent EUR/JPY and USD/JPY decreases at 132.29 and 106.19 respectively (-0.89% and -2.38% last week – the week before: 133.30/-2.88% and 108.80/-1.24%) are alarming.

The fact that Japanese leaders decide to maintain an expansionary monetary policy at all cost will be a way to counter any excessive yen appreciations and preserve Japanese competitive advantage against international peers.

We remain confident that Japanese fundamentals remain solid to face coming currency challenges, keeping in mind that such moves could be seen very badly by Trump administration who could take additional protectionist and trade measures against Japanese counterparts, perceiving an "artificial" weak yen as unfair.



Themes Trading

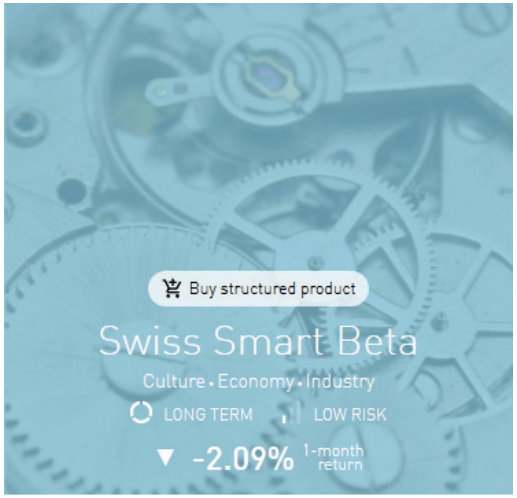
Swiss Smart Beta

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.

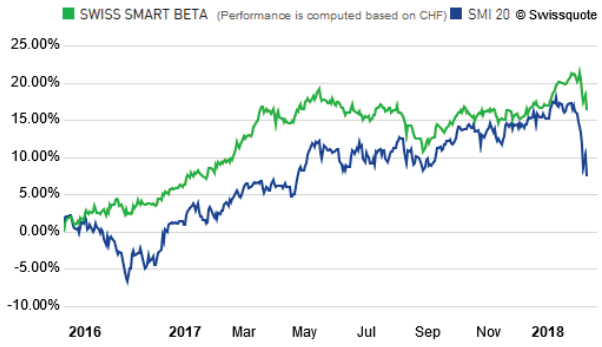
Swiss Smart Beta Certificate is available for trading at :

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

See portfolio details | Buy structured product



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