

# WEEKLY MARKET OUTLOOK

20 - 26 August 2018

## WEEKLY MARKET OUTLOOK - An Overview

p3	<b>Economics</b>	INR Catches the "Cold"- Peter Rosenstreich
p4	<b>Economics</b>	ZAR Fragile, As Further Pressures Are Hitting TRY - Vincent Mivelaz
p5	<b>Economics</b>	Is EUR/CHF Sell-Off Over ? - Arnaud Masset
	<b>Disclaimer</b>	

## Economics

## INR Catches the "Cold"

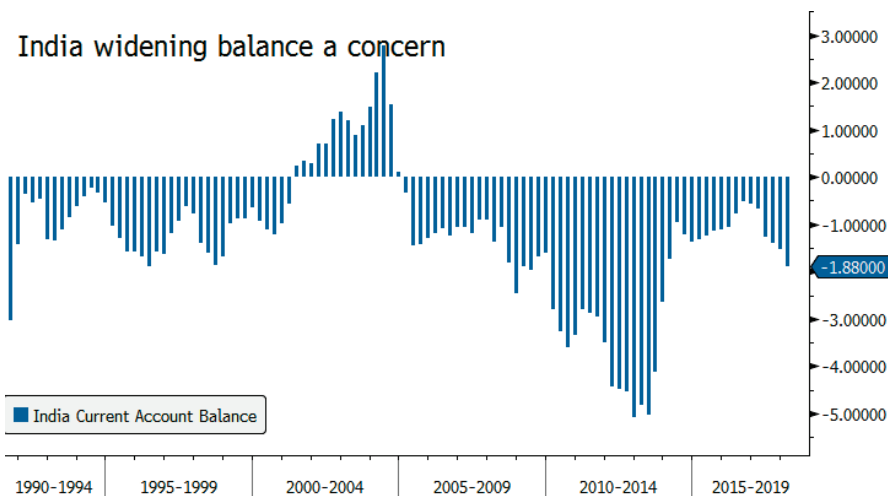
"Only when the tide goes out do you discover who's been swimming naked." - Warren Buffet

While EM currencies are cooling after epic blown-out, INR continues to weaken. USDINR remains above the 70 on Friday. Clearly, Turkish lira contagion played a significant role in turning sentiment negative on the INR, however, the sustained selling indicates there are other issues the markets is not willing to overlook (also see ZAR). India has been bundled together with countries having a "twin deficit". The issue cause further INR weakness is that currency weakness aggravates existing trade imbalances, which is viewed as a fundamental flaw.

The steady INR weakness can be attributed to last week's greater than expected trade deficit, which widened to a 5-year high. Imports surged 29% to \$18bn in July. The rise in imports could be traced to higher oil prices and increase in gold imports (due to lower gold prices attracting bargain hunters). The concerning number overshadowed a strong export read which rose 14%, continuing an elevated 3-month moving average trend. Current account deficit for the fiscal year 2018-2019 could grow to around 2.6-3% of GDP against 1.9% in the prior fiscal year. Moving forward the wider current account deficit are a stress point for international investors. Countries highlighted by traders as "twin deficit" risks continue to underperform within the EM FX space.

RBI's minutes of the August monetary policy meeting indicate that the committee has shifted towards a hawkish bias. The minutes were light on new information however, hawks majority remain confident of the economic recovery and, despite weaker food prices, expect inflation to further trend higher. The 3-month INR OIS rate increased following the release of the RBI minutes indicating a 76% probability that another 25bp hikes will be coming in the next 3-months.

We suspect that the strong overall fundamentals will keep the INR rout from deepening. Yet should pressure increase, we could also see the RBI to increase FX intervention to smooth INR weakness. We could see RBI step-in with additional measures outside of hikes as excessive INR weakness will exacerbate inflations and current account deficit.



## Economics

## ZAR Fragile, As Further Pressures Are Hitting TRY

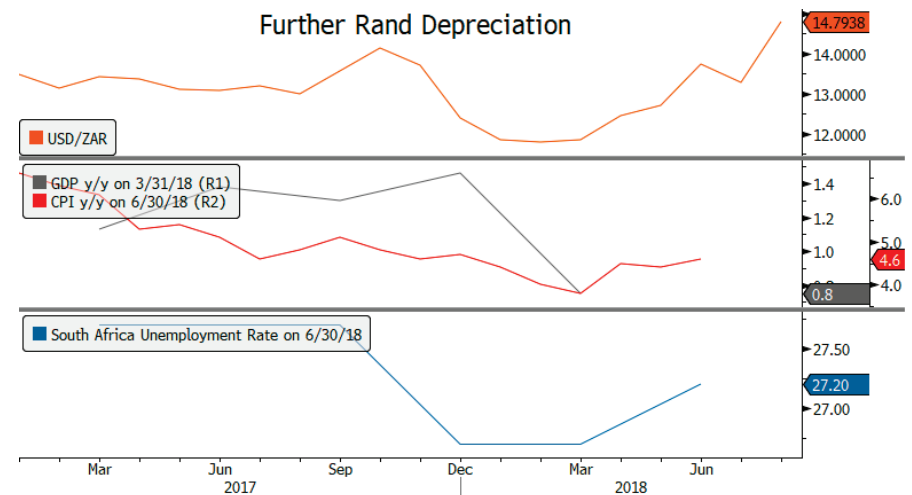
Although TRY downward pressures paused in the middle of last week for three full days, the ZAR, though to a lower extent, has been heading downward for almost the whole week, posing the question of whether or not the South African rand is not going to be the next currency crisis this week. Since the beginning of the year, the currency devaluated against the greenback and the single currency by -19% and -14% respectively.

Indeed, economic growth remains weak, while 1Q 2018 current account deficit estimated at \$ -19.40 billion and deepening since Q4 2016 remains a trouble point, as South Africa's main source of exports relies on commodity prices, for which further decline is not to be overlooked. This is especially the case for precious metals, which account for more than 15% of total exports in the country. South African June gold production data continues to sink, while gold prices reach January 2017 dips. Additionally, as domestic consumption remains low and unemployment rate continues to increase, the South African Reserve Bank (SARB) is having a hard time to stimulate the economy.

Recent political decision to expropriate wealthy landowners owning more than 12'000 hectares of lands without financial compensation along with continued delay in South African budget consolidation amid poor tax revenues remain major stumbling blocks for the South African nation, pushing important downward pressure on the rand.

Accordingly, the SARB decision, unlike the Turkish Central Bank, whose independence is undermined, has to react properly given the current economic situation. Inflation remains stable and undershoots current 3 – 6% target band while expectations of weaker growth makes a rate hike during 20. September 2018 MPC less likely. SARB Deputy Governor Daniel Mminele statement that no interventions are required as long as the market is working smoothly says a great deal to that regard.

South African rand, similarly to Turkish lira, is expected to decline further, but at a much lower pace though. The key difference lies in the fact that SARB independence is not questioned. Therefore, currently trading along 14.80, USD/ZAR is expected to approach the 15 range, as investors' fears of contagion are slowly fading.



## Economics

## Is EUR/CHF Sell-Off Over ?

Over the last few days, the Swiss franc made a solid come back in the wake of worsening crisis in Turkey and mounting worries that it would spark emerging market contagion. After falling more than 5% in early summer as Italy's elections damaged further European unity, EUR/CHF fell another 4% over the last month amid persistent trade war tensions between the US and its main trading partners, as well as worries that the Turkish crisis could damage European banks.

In addition, over the next few weeks markets will turn their focus back on Italy. The new government is expected to provide a budget plan for 2019 indicated how closely officials would stick to their expensive spending promises. Any extreme unfunded deficit spending plan will likely add to domestic turmoil and conflict with the EU. For now, it looks like the Italian government has adopted a cautious approach – to avoid scaring international investors away - as it declared it is committed to debt reduction.

Against such a backdrop, there is no doubt the Swiss National Bank has had a stressful summer so far as investors returned to the Swiss franc, and safe-haven assets in general. However, according to the SNB's weekly report, the central bank hasn't intervened in the FX market since July 2017. Total sight deposits have remained stable around CHF 575bn, with a max at CHF 579.7bn in August last year. In our opinion, the Swiss franc hasn't appreciated enough against the euro to trigger a SNB's intervention. Monday's report will give us the answer. The currency pair currently stands at 1.1360, which is well above the implicit 1.05 "floor". In addition, the euro sell-off looks overdone and the easing tensions between China and the US could only help to improve the overall risk sentiment. Even though we remain cautious in the short-term, EUR/CHF can go only go up in the medium to long-term.

EUR/CHF under pressure



## DISCLAIMER

While every effort has been made to ensure that the data quoted and used for the research behind this document is reliable, there is no guarantee that it is correct, and Swissquote Bank and its subsidiaries can accept no liability whatsoever in respect of any errors or omissions, or regarding the accuracy, completeness or reliability of the information contained herein. This document does not constitute a recommendation to sell and/or buy any financial products and is not to be considered as a solicitation and/or an offer to enter into any transaction. This document is a piece of economic research and is not intended to constitute investment advice, nor to solicit dealing in securities or in any other kind of investments.

Although every investment involves some degree of risk, the risk of loss trading off-exchange forex contracts can be substantial. Therefore if you are considering trading in this market, you should be aware of the risks associated with this product so you can make an informed decision prior to investing. The material presented here is not to be construed as trading advice or strategy. Swissquote Bank makes a strong effort to use reliable, expansive information, but we make no representation that it is accurate or complete. In addition, we have no obligation to notify you when opinions or data in this material change. Any prices stated in this report are for information purposes only and do not represent valuations for individual securities or other instruments.

This report is for distribution only under such circumstances as may be permitted by applicable law. Nothing in this report constitutes a representation that any investment strategy or recommendation contained herein is suitable or appropriate to a recipient's individual circumstances or otherwise constitutes a personal recommendation. It is published solely for information purposes, it does not constitute an advertisement and is not to be construed as a solicitation or an offer to buy or sell any securities or related financial instruments in any jurisdiction. No representation or warranty, either express or implied, is provided in relation to the accuracy, completeness or reliability of the information contained herein, except with respect to information concerning Swissquote Bank, its subsidiaries and affiliates, nor is it intended to be a complete statement or summary of the securities, markets or developments referred to in the report. Swissquote Bank does not undertake that investors will obtain profits, nor will it share with investors any investment profits nor accept any liability for any investment losses. Investments involve risks and investors should exercise prudence in making their investment decisions. The report should not be regarded by recipients as a substitute for the exercise of their own judgment. Any opinions expressed in this report are for information purpose only and are subject to change without notice and may differ or be contrary to opinions expressed by other business areas or groups of Swissquote Bank as a result of using different assumptions and criteria. Swissquote Bank shall not be bound or liable for any transaction, result, gain or loss, based on this report, in whole or in part.

Research will initiate, update and cease coverage solely at the discretion of Swissquote Bank Strategy Desk. The analysis contained herein is based on numerous assumptions. Different assumptions could result in materially different results. The analyst(s) responsible for the preparation of this report may interact with trading desk personnel, sales personnel and other constituencies for the purpose of gathering, synthesizing and interpreting market information. Swissquote Bank is under no obligation to update or keep current the information contained herein and not liable for any result, gain or loss, based on this information, in whole or in part.

Swissquote Bank specifically prohibits the redistribution of this material in whole or in part without the written permission of Swissquote Bank and Swissquote Bank accepts no liability whatsoever for the actions of third parties in this respect. © Swissquote Bank 2014. All rights reserved.