Weekly Market Focus

12 July 2017

HINDUJA BANK

SWITZERLAND

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ASSET CLASS REVIEW

Even though it is almost ten years since the global financial crisis, fixed income investors are starting to find traditional markets unattractive with low yielding bonds. US and European investors are therefore under pressure to find investment ideas that offer attractive yields and total return potential.

Indian Bonds

India offers one such opportunity; it is a large and attractive fixed income market offering high-single digit local currency yields, with a solid country credit profile, a sizable number of domestic corporate and provincial credits and a track record of attractive returns. In addition, given India's current position in its developmental trajectory, we believe that Indian fixed income markets offer a long runway for investors in terms of returns, making the time and effort spent to acquaint themselves with them highly worthwhile.

Investors often cite diversification as an advantage of multi-country Emerging Market Debt exposure. While this argument is valid when the single country exposure is from a small country with less diversified economy, it loses its merit in the context of India - a well-diversified, continent sized economy with a large and growing government and corporate debt market. India is also home to many companies with a global footprint. Their credit characteristics are strong enough for many of them to be rated higher on stand-alone basis than India's BBB- sovereign rating.

Just a few years back, Morgan Stanley included India among a group of five fragile currency countries in the world. This is no longer the case.

As of December 2016, three original "fragile five" members, South Africa, Turkey and Indonesia, have been joined by Mexico and Colombia, who replaced India and Brazil.

India ranks high in terms of institutional stability. It has a free press, a functioning legal system, and a vibrant democracy. In Prime Minister Narendra Modi, the country has a visionary leader who has embarked upon an ambitious economic reform agenda. The ruling BJP's landslide win in the Uttar Pradesh (UP) assembly elections earlier this year has improved the prospects of yet another five-year term for Prime Minister Modi. UP, after all, is the largest state in India and the BJP succeeded in increasing its vote share there across class, caste and Communities. With a strong possibility of an extended rule to 2024, the Bharatiya Janata Party is in a position to deliver on a number of reforms that are in the pipeline.

As a result of the completed and anticipated reforms, India is scheduled to be the fastest growing major economy in the world, easily overtaking China. In Purchasing Power Parity (PPP) terms, India is already third in the world. The rapid rise in working age population together with on-going economic reforms should propel India upwards in the coming years. At the same time, India is set to keep inflation below 5%. Barring a sharp rise in commodity (oil) prices, the current account deficit is expected to stay well below 2% of GDP from 2017 to 2019 on average. Finally, the BJP government has also renewed its commitment to stay on the fiscal consolidation path and cut the fiscal deficit to 3% of GDP in the next three years.

Despite these improvements in economic management as well as outcomes, India's credit rating has stayed at BBB-. The rating agencies, as usual, have been slow. The assessment of the markets, however, has increased sharply since early 2014. The five-year CDS spread has dropped from upwards of 275 in early 2014 to well under 100 at present.

Indian fixed income market is an attractive opportunity as it has expanded in terms of variety and size of the instruments. The market has also become increasingly liquid and open to foreign portfolio investors. Relative to its peers, India offers a rare combination of political stability, rising growth, falling inflation and declining fiscal deficit. The current government (the first in over thirty years to have a single party majority rule) has implemented several bold structural reforms that are set to reduce fiscal deficit further in a sustainable manner.

FOREX

NFP data beat expectations last Friday, but offered little to lift USD bullish confidence. Employment came in with an extra 222k (expected 178k) new jobs been added to the economy.

USD

Nevertheless, for the Fed too inflation remains the key issue, it being too low, hence FOMC talk warrants close attention. The next inflation data for the US is PPI. Historically not a market mover, but an important piece of the puzzle. Friday brings CPI data where expectations rotate around 1.7% YoY. The highlight this week will be Yellen's testimony before the senate committee, (previously aka the HH testimony). Fed noise has been mixed recently but one note chimes through the FOMC; that one more hike is correctly priced by the market. Yellen erred on the hawkish side in her last delivery, so expect her testimony to be USD supportive.

EUR

Summer doldrums, what to say. Technically, EURUSD still has its eyes on the 1.1460 resistance line. Prices should remain capped here over the near term. Prices to the downside are supported by the June/July recent trend and the pivot at 1.1285/95. The medium term trend is strong here and should be respected. We like the majority of market participants prefer to buy on dips. Support below 1.1285 can be found at the pivotal TL at 1.1180 and 55 mda at1.1165. Below that the May/June lows at 1.1110/20 will be met with demand.

Core theme, play the range.

GBP

Sterling has been range bound having failed to maintain prices above 1.3000 handle. Considering the present back drop. We don't see prices extending too far in either direction beyond the 1.3050/1.2850 range. Recently we have seen a pick-up in inflation and a more hawkish rhetoric from some BoE voting members the latter indicating a possibility of a 5-4 spilt at the next MPC meeting. This week we see labour data where wages pressure data will be closely watched. The following week brings CPI. The inflation theme not just focuses on the recent pickup in headline inflation, but to see if this carries through to earnings growth.

If we see a low print, this expresses the rise in inflation is merely transitory and the resulting real income squeeze will weigh on consumer spending.

Rates markets discount a 40% probability of a 25 bps hike on the forward SONIA curve by year end. The Dec Short Sterling future having corrected 17 ticks lower in June now consolidates in a bear flag pattern. Probes higher to 99.55 (200mda) to 99.58 Trend channel resistance will be met with good supply. Prices should extend lower here to 99.41/42.

For FX, **We are still bullish for GBP and prefer to buy on dips at 1.2820/40 against the USD.** GBPJPY looks expensive testing again the 148.00 pivot. Divergence is emerging on the charts suggesting a near term correction threatens the bullish case.

EURGBP currently tests key resistance at 0.8860/70. This area marks the 50% Fibo of the Oct16/Dec16 down move, and has been key resistance going back to Jan this year. Momentum indicators suggest divergence.

CAD

Big week for Canada. Rates markets discount a 90% probability of a 25 bps move to 0.75% Wednesday. Risk reward suggests being long USDCAD into the decision will see a sharp move higher towards 1.3030 resistance on a dovish move. Canada bulls will need to digest the BoC statement for indications of further hikes or if this move is a 'one and done'.

USDCAD has been consolidating just above the 1.2860 low following the strong labour data on Friday. Options markets, being prudent, have however seen interest to buy short term upside protection structures considering market position ahead of the BoC, as noted above.

Market consensus for a hike at 90% clearly reflects BoC rhetoric of late, having done a U-Turn on policy during June.

Positioning will be tough for the rate decision to position for via cash, considering the binary outcome. On a no move, we spike to 1.3100 only to retrace lower as markets merely shifts rate expectations down the curve. One hike and done sees USDCAD retrace higher to 1.3030/50 resistance and sticks. Or thirdly we get a 25-50 bps hike and indications of further hikes from the central bank. This last scenario will see CAD strengthen to 1.2760/70 against the USD.

JPY

Recent announcements from the BOJ with regards to maintaining long term rates close to zero and suggesting a new approach to ease again have weighed on the JPY. We wrote that the JPY is our favoured short over the medium term as other key central banks talk of ending easing policy and a return to normalisation while the BOJ remained unmoved. Therefore yen weakness came as no surprise when BoJ governor Haruhiko Kuroda underlined once again that the central bank was willing to continue its easing approach, despite its ‘white elephant’ of a 2% inflation target. This is not new news for the markets, but a kind reminder.

So continue to buy x JPY dips, 113.40/60 against the USD for example. Some caution is warranted here, using the charts as a guide GBPJPY, CADJPY and EURJPY are all stalling at key pivot resistance points.

In summary, markets now see that the BOJ will be the only G10 central bank not starting a rate normalisation process at the latest by next year, a justified reason to sell JPY.

CHF

EURCHF finally moves. Markets seem content to sell safe haven trades, Gold, US treasuries, and now CHF. EURCHF has out done itself in trading through 1.1000 and now is within a hare breath of the 1.1067/70 76% Fibonacci resistance zone. Again, normalisation of rates plays a key role in the FX move as the SNB has left itself as the ‘lone dove’ in Europe. The central bank will welcome the move as now it needs to do less to achieve its aim of a weaker currency. Further downside for the Swiss currency is in store and we now see the cross moving into a new range above 1.0920.

After it broke through a key technical level at 1.10 per euro on Monday and dropped to its lowest since June 2016.

Technically we do not envisage much further upside in the near term through 1.1050 as technically we have seen 12 higher days suggesting exhaustion.

VIEWS FROM THE TRADING FLOOR

Equity

S&P was down 0.14% on the last week, with a decrease in volatility, VIX finishing the week at 10.78 from 11.22. On the upside we found semiconductor up 10% while electronic equipment and instrument was up 6%. On the down side the biggest fall is for automotive retail industry down 13% followed by computer & electronics retailers down 9% and home furniture's retailers down 8%.

In the US the focus this week will be on the June consumer price index released on Friday Market currently believes that Fed cannot or will not continue its monetary policy normalization as announced owing to the just moderate price buoyancy. These speculations should again be fueled on Friday. In the past month, consumer prices are likely to have risen by a 0.1% mom according to the consensus which, according to Raiffeisen should result in a decrease in the year-on-year rate from 1.9% to 1.7%.

S&P 500: The first support area 2400-2387, is still holding but no clear rebound as taken place yet. If this first support is broken on a close basis then there 2350 will be tested and probably 2325 will be tested too. On the upside 2453 is the first target a break above this level will lead directly to the first target area 2484-2500.

Eurostoxx 50: The index is evolving in its new trading range 3525-3435. With a quite low volatility at the moment as there is no key driver. A close below 3435 will open the way to a test of the strong 3400 a close below this level will immediately lead to 3325. A break above 3525 will fuel a rise to 3600.

EQUITY

Developed countries

		Total return - 1 Week
SMI	↓	-0.4%
Euro Stoxx 50	↓	-0.2%
DAX	↓	-0.1%
FTSE 100	↑	1.8%
S&P 500	↑	0.1%
Dow Jones	↑	0.3%
Nikkei 225	↓	-0.4%

Developing countries

Russia/Micex	↓	-1.5%
India/Nifty 50	↑	1.3%
China (HK)	↑	1.4%

↑ - Upward move ↓ - Downward move

FIXED INCOME

Developed countries

	2-year Yield	10-year Yield
USA	1.3%	2.3%
UK	0.1%	1.1%
Germany	-0.7%	0.4%
France	-0.4%	0.8%
Italy	-0.3%	2.2%
Spain	-0.3%	1.6%
Switzerland	-0.9%	-0.1%

Developing countries

	2-year Yield	10-year Yield
Russia	2.3%	4.3%

COMMODITIES

		Total return - 1 Week
Crude Oil	↓	-7.2%
Gold	↓	-3.0%

CALENDARS

Economic Events

Date of release	Domicile	Event	Period	Actual	Estimated
13 July 2017	US	Initial Jobless Claims	08 July 2017	245k	248k
14 July 2017	JN	Industrial Production MoM	May F	--	-3.30%
14 July 2017	US	CPI MoM	Jun	0.10%	-0.10%
18 July 2017	UK	CPI YoY	Jun	--	2.90%
18 July 2017	EC	CPI YoY	Jun F	--	1.40%
18 July 2017	GE	ZEW Survey Expectations	Jul	--	18.60

Company Earnings

Date of release	Domicile	Company Name	Period	Estimate EPS
14 July 2017	US	JPMorgan Chase & Co	Q2 17	1.59
14 July 2017	US	Citigroup Inc	Q2 17	1.21
17 July 2017	CH	SGS SA	S1 17	39.62
17 July 2017	US	BlackRock Inc	Q2 17	5.36
18 July 2017	US	Johnson & Johnson	Q2 17	1.79
18 July 2017	US	Lockheed Martin Corp	Q2 17	3.11
18 July 2017	US	Goldman Sachs Group Inc/The	Q2 17	3.47
18 July 2017	CH	Novartis AG	Q2 17	1.18
18 July 2017	US	International Business Machines Corp	Q2 17	2.74
19 July 2017	US	QUALCOMM Inc	Q3 17	0.85

Contacts

Geneva – Headquarters

Hinduja Bank (Switzerland) Ltd

Place de la Fusterie 3bis
1204 Geneva, Switzerland
Tel. +41 58 906 08 08
Fax +41 58 906 08 00

Branches

Zurich
Florastrasse 7
8008 Zurich, Switzerland
Tel. +41 58 906 05 05
Fax +41 58 906 05 06

Lugano
Viale Serafino Balestra 5
6900 Lugano, Switzerland
Tel. +41 91 910 43 43
Fax +41 91 923 55 73

Representative Offices

London
Amas Investment &
Project Services Ltd
Room no: 117,
First Floor, Regus,
100 Pall Mall,
London SW1Y5NQ
Tel. +44 20 7321 5642

Paris
Rue Galilée 33
75116 Paris, France
Tel. +33 1 44 43 52 36
Fax +33 1 40 70 03 79

Subsidiaries

Switzerland
Berafina AG
Münchensteinerstrasse 43
4001 Basle, Switzerland
Tel. +41 61 225 45 45
Fax +41 61 225 45 25

Rowena AG
Grenzstrasse 24
9430 St Margrethen, Switzerland
Tel. +41 71 747 49 59
Fax +41 71 747 49 51

Dubai
Hinduja Bank (Middle East) Ltd
Dubai International Financial Centre
Building GV 10, 2nd Floor, Unit 5
Dubai, UAE 506783
Tel. +97 14 436 65 88

Mauritius
Hinduja India Mauritius Holdings Ltd
HBS Trust Services (Mauritius) Ltd
1st Floor, Manor House Cr. St. James
Chazal Street Port Louis, Mauritius
Tel. +230 208 75 75
Fax +230 208 75 74

USA
Hinduja Capital Advisors Inc
520 Madison Ave., 34th Floor
New York, 10022, USA
Tel. +1 212 355 07 55
Fax +1 212 752 73 12

UK
Amas Investment & Project Services Ltd
Room no: 117,
First Floor, Regus,
100 Pall Mall,
London SW1Y5NQ
Tel. +44 20 7839 4661
Fax +44 20 7839 5992

India
Paterson Securities Pvt Ltd
Bhavani Mansion 3, 4th Lane
Nungambakkam High Road
Chennai - 34
India

Cayman Island
Hinduja Bank & Trust (Cayman) Ltd
c/o P.O. Box 2407GT
Grand Cayman
Cayman Islands

Publisher

Hinduja Bank (Switzerland) Ltd

Place de la Fusterie 3 bis

1204 Geneva, Switzerland

Tel. +41 22 906 08 08

Fax +41 22 906 08 00

www.hindujabank.com

info@hindujabank.com

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