Weekly Market Focus

HINDUJA BANK SWITZERLAND

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ASSET CLASS REVIEW

We are slowly running out of superlatives to describe the global economy. The economic data in November were once again strong and mostly sprang positive surprises. In the US there is a good chance that gross domestic product (GDP) growth will be at 3% or more in the fourth quarter of 2017 as well, for the third consecutive time. The economy in the euro-zone is also very favourable, and in most emerging markets the trend is at least satisfactory. The upswing continues to be accompanied by tame inflation. In such a climate, equities remain more attractive than bonds.

Global Economy

The global economy picked up further momentum and will end the year with accelerating growth. The increase in global trade, an expansive monetary policy and, in particular, the economic consequences of the political agenda were fertile ground for this in 2017. In the euro- zone the specter of euro-skepticism was banished with the election of Emanuel Macron. China's government further stimulated the economy, and the fact that the Trump administration did not deliver on its promises has its good aspects. For example, the Trump administration's protectionist posturing vis-àvis the rest of the world had no impact. Another important factor in the economic acceleration in 2017 was the combination of interest rate normalization in the US accompanied by the depreciation of the US dollar. The trade-weighted dollar dropped by 8% since the beginning of the year as a result of mounting skepticism about the Trump administration, even though the Fed raised interest rates further. This created a favourable climate for the commodity market, emerging markets and, finally, Europe.

For 2018, the outlook still looks encouraging.

The economic upturn will continue in 2018, and inflation is likely to rise. Although we consider the global inflation risk still to be low, in the US economists believe that the ingredients for heightened price pressure are assembled. There are many indications that the US has entered a late phase of its economic cycle. The output gap is closed, there is full employment and the Fed continues to normalize monetary policy. The dried-up US labor market is likely to result in rising wage pressure. Higher prices for raw materials – particularly energy will also contribute to a rise in inflation. The weaker US dollar means that imports will be more expensive.

This signals that the US economic cycle is becoming more mature. One should nevertheless anticipate a slight acceleration in the US. Investment momentum is increasing, and consumption is still robust. Corporate tax reform may provide an additional boost.

The rest of the world is lagging behind the US economic cycle and thus still has considerable catch-up potential. In Europe and the emerging markets, economic growth also continued in 2017, and thus the European Central Bank (ECB), the Bank of England (BoE) and the People's Bank of China (PBoC) were able to start preparing for the end of the ultra-expansive monetary policy. This must be put into perspective for the ECB as the bond purchasing program will continue until at least autumn 2018 in reduced form (as of 2018 EUR 30 billion instead of EUR 60 billion per month). Nevertheless, the euro appreciated, which is why we should expect a slight slowdown in economic momentum in the euro-zone. The euro-zone, like the US, is supported by a prospering domestic economy. However, deleveraging in China is likely to cost somewhat more GDP basis points. The tightening of monetary policy underway since mid-2017 and the Chinese government's focus on qualitative growth are likely to result in a slowdown in GDP growth. However, this is an important, positive step for China's financial stability. Against this backdrop, we do not rule out that China may cause an increase in volatility on the markets. However, this will not cast doubt on the structure of the global economy.

FOREX

The USD has benefitted from higher US long rates following late Friday's news of the US tax bill passing, USDJPY benefitting the most. Scepticism remains however over longer-term growth prospects later in the cycle. Front-end rates continue to tighten as priced off the Fed funds curve. The USD STIR curve now prices a 22% probability of rates ending 2018 at 2.25%. This falls in line with Fed rhetoric chiming with their moderate hawkish tone. The USD trades better amid these dynamics but seems reluctantly bullish from here. High beta complex still trading poorly with commodities mixed. DXY holds just above the 93.00 handle. Resistance to the upside at 93.50 support 50s pips lower at 92.50. Risk sensitive crosses remain supported such as AUDJPY which is currently capped by the 200 mda resistance line. Nevertheless from here it appears to be a 'fait accompli' that the uptrend continues.

EUR

Not much to report from the Eurozone of late with EURUSD price action driven by the USD side of the cross. Recent market attention has focused on STIR markets. The daily fixing for the EONIA market tightening by 10 bps. The rumour mill was busy in its search for answers but towards the end of the week the spike in the fixing may have been the result of excess liquidity injected into the market by Greece's second-biggest lender at above-average rates. EURUSD barely budged but front-end rates nudged up slightly as a result. Other news, Germany is calling for an end to QE beyond Sep 2018 which is causing some concern within the ECB. The Bundesbank are worried higher inflation in Germany. This may raise again the question of the 'one policy does not fit all' issue. EURUSD consolidates while rotating around the 1.1880 pivot. Prices just about remain in the recent Nov bullish channel upswing with first support at 1.1780/90. **The Euro has twice now tried to trade above 1.1950 but failed leaving 1.1960/70 as key resistance. At the present juncture we prefer to watch and see for future market direction.**

GBP

What a difference a week makes. Cable traded a 2.5% range last week, mainly been driven by Brexit news. Having briefly touched a low of 1.3221, it traded higher to touch a new interim high at 1.3549. Factors contributing to the volatility is ongoing as progress is slowly being made on EU/UK Brexit negotiations, with Junker even sounding mildly optimistic and upbeat. British PM Theresa May and the president of the EU Commission Jean-Claude Juncker had come to a first agreement in the Brexit negotiations. As mentioned last week the current milestone is the Northern Irish border question. Remember the UK government is a coalition with NI DUP political party, strong Unionists keen to remain full separated from the republic and the EU. The Irish government demands that the border remains open and currently is lobbying hard in Brussels to veto any agreement other than this. The UK and EU representatives had agreed that the same rules should apply in the Republic of Ireland and in Northern Ireland to avoid a hard border. The DUP however rejects the idea of different regulations between Northern Ireland and the rest of the United Kingdom, therefore blocking the British government's proposal. We do feel though that it is just a matter of time before agreements take place, therefore we continue to favour buying pound dips towards 1.3330/40 against the dollar. Domestically, UK data has been good. UK manufacturing PMIs beat expectations however Services PMI dipped to 53.6, eroding the previous month's gain at 55.6. Cable shrugged off the weaker Services PMI data preferring to focus on Brexit headlines.

Last week cable closed just above the 2014/2017 downtrend indicating higher prices are in store. From a weekly perspective, despite the retracement lower to 1.3430/35 amid Brexit noise, upside momentum remains well in place. It would take a weekly close below 1.3220 to negate the upswing. Looking at the daily charts, intraday movements remain volatile. We approach the market with caution preferring to wait for extremes, and err on the lower side of the ranges before assuming upside risk. Retracements back towards the 55 mda at 1.3270/80 should be taken as a buying opportunity risking 1.3220. Trading needs to be nimble and disciplined for the pound intraday. To the topside immediate resistance awaits at 1.3511. **A close above here would be welcomed by sterling bulls opening the way for 1.3657 and 1.38 upside targets.**

USD

The USD is becoming ever more sensitive to political noise in the US. Late on Friday before the tax bill had been passed by the Senate, news that ex Security advisor Flynn having already admitted to the FBI of lying, would testify that president Trump directed him towards Russia. Safe haven assets quickly gained on the news. The CHF and JPY especially strengthening against the USD. These gains were later reversed on the Tax bill announcement. This week, in the wake of the Tax Bill and as we approach NFP on Friday we expect further relief for the USD overshadowing negative news. Regarding the bill, The US Senate finally passed a major legislative measure in the shape of the tax reform bill. This story does not end here however with more hurdles still having to be overcome before year end. The representatives have to agree on the expiring funding authorisation for the Federal government to avoid a government shutdown. Memories of previous scenarios will be a concern for FX markets and will weigh on the USD. The week's main economic release is on Friday, the November NFP US labour market report. Market consensus looks for the headline nonfarm payrolls to show an addition of 200K jobs, down from October's 261K reading. As always, extra focus will centre on the average hourly earnings growth where a slowing to 0.3% is expected.

JPY

USDJPY volatility spiked last week as the cross tested both the upper and lower bounds of recent ranges and the 'Ichi-Moju' technical cloud, see chart. Having bounced from the 111.00 pivot support, prices rose to above 113.00. The sharp swings can be attributed to US political noise and in turn volatility in long end US rates. The yield on the US 10 year is capped at 2.50% capping 10yr yields, and as such, the upper end of the USDJPY range looks less likely to exceed 115.00 over the near term. Data-wise Japanese GDP for Q3 is due out on Thursday. A figure of 1.5% is expected with little JPY movement as a result. Growth is picking up pace, however the BOJ are not expected to adjust monetary policy over the medium term. Support is at 111.40/50 guarding critical support at 110.80. To the upside, first levels to be tested are last week's high and cloud resistance at 113.10. Above that 114.50 is pivotal as a break through there could result in USDJPY moving into a new range of 115/118, the late 2016 highs. **We favour buying dips below 112 with stops below 111.40. First upside target is 113.10 and above that 114.00**.

AUD

We wrote last week about the AUD and our preference to buy it. This had gone against news emanating from Australia that the RBA has managed to prevent further AUD appreciation by stressing the risks of a strong currency for its inflation and economic outlook. In its statement this morning the central bank weakened its rhetoric on the exchange rate and generally seemed more relaxed with lower inflation levels. FX markets took comfort in this to indicate that a strong AUD now seems more probable. Other news for the Aussie saw the OECD last week speaking in favour of a rate hike in Australia due to rising household debt levels. The labour market data in Australia remains steady, judging by recent economic data published last week. The RBA still considers the weak wage growth to be the main reason for the low inflation levels and consequently is slow with monetary policy normalisation. Technically AUDUSD remains in the weekly bull channel from the beginning of 2016. It has recently bounced off this trendline close to 0.7530/40. There is negative divergence when measured against weekly momentum, so some caution is warranted here. A close above the 55 weekly average price line at 0.7655 is needed to confirm that the upside bias still remains. Over the short term, a break through 0.7650 will see prices quickly extend to 0.7700 where there is a convergence of 200 and 55 MDA resistance. AUDUSD pricing now is comfortably above the Sept/Nov bear trend and RSI and momentum indicators are gaining.

We favour buying AUDUSD at 0.7610/20 risking a close below 0.7550. Initial upside targets are at 0.7750 and above that at 0.7815 where Fibonacci cluster resistance will impede further gains.

Wednesday sees the Bank of Canada's (BoC) interest rate decision, with the majority of market economists calling for an unchanged outcome, leaving the key interest rate unchanged at 1.00%.
The central bank has raised rates twice already in Q3. Current interest rate pricing for the meeting attaches only a 20% probability of a 25 bps hike.
Governor Poloz has sounded more cautious in recent addresses, highlighting that it expected the economy to slow (GDP growth moderated to 1.7% in Q3 on a Qtlry annualised basis, from 4.3% in Q2) while stressing that it remains data dependant.
The BoC remains focused on the consumer's reaction to previous hikes maintaining its wait-and-see approach for the moment. Wage growth, like other central banks, is a key issue with the latter having improved in recent employment reports The core scenario is still that the BoC underlines the need that less monetary stimulus will likely be required over time.
Last week USDCAD fell following strong GDP and payrolls numbers. The Loonie fell marking a double top formation from 1.2917 down to monthly support at 1.2520. Prices have since consolidated as markets await the BoC decision. We prefer to stand aside for this cross. Downside momentum presently is the path of least resistance with next support just below 1.2500. Upside resistance awaits at 1.2904, last week's high, and just above that at 1.2975/80, the 200 mda.

VIEWS FROM THE TRADING FLOOR

Equity

S&P was up 0.1% on the last week, with volatility rising from 10.03 to 11.67. On the upside, we find fodd retail up 11%, department stores and railroads up around 8%. On the down side, semiconductor equipment were down 12% while home entertainment software and health care suppliers were down 8%.

In the US, the focus this labour market report for November that to be released on Friday. According to Raiffeisen, the substantial deflections in employment growth that arose in September and October should thus not continue. They assume that 177k new positions were filled in November. This makes them somewhat more cautious than the consensus, which on average anticipates a plus of 195k. They however forecast that the hitherto reported 261k rise for October to be revised upwards. The unemployment rate is likely to have kept its 17-year low of 4.1% reached in October.

S&P 500: The index is slowly but surely continuing its advance toward the 2710 target. This trend will remain in place as long as 2590 remains a support. Any correction occurring should target the 2600-2590 area. A break below this level will then target 2510 and 2484 levels.

Eurostoxx 50: the index is evolving in a 2% trading range between 3525 and 3600. A break above 3600 will lead to 3666 and possibly 3700. On the downside, 3525 remains the key support. Below this level, the next significant support stands at 3500 before 3450.

EQUITY

Developed countries

		Total return - 1 Week
SMI	↓	-0.2%
Euro Stoxx 50	↓	-0.5%
DAX	↓	-0.1%
FTSE 100	↓	-0.9%
S&P 500	↑	0.2%
Dow Jones	↑	1.1%
Nikkei 225	↓	-1.9%

Developing countries

Russia/Micex	↓	-0.7%
India/Nifty 50	↓	-2.8%
China (HK)	↓	-4.3%

↑ - Upward move ↓ - Downward move

FIXED INCOME

Developed countries

	2-year Yield	10-year Yield
USA	1.8%	2.3%
UK	0.5%	1.3%
Germany	-0.7%	0.3%
France	-0.6%	0.6%
Italy	-0.4%	1.7%
Spain	-0.4%	1.4%
Switzerland	-0.9%	-0.2%

Developing countries

	2-year Yield	10-year Yield
Russia	2.4%	3.9%

COMMODITIES

		Total return - 1 Week
Crude Oil	↑	0.1%
Gold	↑	-1.1%

CALENDARS

Economic Events

Date of release	Domicile	Event	Period	Actual	Estimated
06 December 2017	US	Nonfarm Productivity	3Q	3.0%	3.3%
06 December 2017	US	Unit Labor Costs	3Q	0.2%	0.5%
08 December 2017	US	Unemployment rate	November	4.1%	4.1%
08 December 2017	Germany	Current Account Balance	October	25.4b	20.0b

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