Weekly Market Focus

HINDUJA BANK
SWITZERLAND

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ASSET CLASS REVIEW

High Volatility

Volatility in the equity markets as well as the continuous rise in government yields was the focal point of attention during the first quarter. It is interesting to note that the selloff in equity markets came at a moment where nearly every financial article and analyst was questioning whether or not the stock valuation was justified. This might be seen as a confirmation of the “self-fulfilling prophecy” theory, which states that when a large group of people believe of fear an event, this event would ultimately happen.

From a more academic point of view, even with some retrospect, it is impossible to exactly determine what exactly provoked this sudden rise in volatility. Some reasons however seem to be the most likely:

■ The acceleration of the rise in inflation. This is one of the most often cited reasons. The wages and CPI figures seem to confirm the rise in the level of prices. The term “inflation” appear to be searched more and more often on Google, as showed by Google Trends, maybe a sign that the general public is feeling its effects and getting more concerned.

■ Treasury auctions. The Federal Reserve issued a weekly record amount of more than a quarter of a trillion USD in short term bills during the week of February 19th. This might become the norm for the month and years to come given the increase in US federal spending, and the large budget deficits the Trump administration is running.

■ Overheating US economy. Some observers argue that the generous government spending coupled with large tax cuts in an economy with nearly record unemployment and operating near the maximum of its productive capacity might lead to an inflation that would spiral out of the Fed’s control and might derail the US economy.

Investor psychology is a key factor

The fact it is difficult to find a rational answer, might lead one to think that investor psychology played an important role in the recent past events and that it will be a key driver for the months ahead. In this nervous climate where emotions are running very high, we believe that financial markets may be at risk of experiencing more punctual selloffs of the kind we saw in January.

European political risk might be underestimated

The political landscape in Europe remains an overhanging risk to market stability. After Germany, which took 6 months to form a government and create a coalition between the CDU, CSU and SPD after the September elections, Italy is in the same political deadlock. After the March elections, none of the three main alliances won an outright majority in the parliament. There is a high probability of months long negotiations between the three main formations, which have unaligned interests and might be unable to find common ground. Even if this is admittedly a regional event and a major one, even if it appears to have no direct effect on the area’s economy and markets, such events, as we witnessed with the Catalonian independency question, create uncertainty and do have repercussion on investors’ confidence globally.

Rates across markets are on a rising trend during Q1, mainly on the back of inflation worries. While this scenario might prevail over the near term, investors should be wary of when sentiment turns and the market starts to focus on the next trend.

FOREX

In the UK, growth fell to a 5yr low in Q1 expanding just 0.1 q/q or 1.2% y/y, weaker than market expectations, outing further pressure on the Pound. This data was the final nail in the coffin for rates markets who now only attach a 19% probability of a rate hike in May, down from 83% a week ago. German bund yields have nudged a little lower on the trading session with some of the softer data out of Europe compounding the effects of the moderation in UST yields. Some consolidation is seen from here as the market takes a breather following the moves in GBP markets and digesting the ECB's view that the slight moderation in growth will be temporary.

EUR

It doesn't look too rosy for the Euro. We have been banging the drum all year with regards to the unjustified weak dollar. Now that we are above key resistance levels of 0.9150 on the Index, major currencies such as the Euro are suffering. The US economy appears to be doing ok with low unemployment, acceptable growth numbers and an inflation rate just shy of 2%. The EZ however seems to be lagging, lower growth and inflation. This combined with technical factors, puts a dent in our former expectation of a EURUSD above 1.2500 for the second half of this year. Fundamental factors such as interest rate differentials, the result of tightening US monetary policy and higher long end US yields, finally seem to be influencing traditional exchange rate direction. The fashionable trade of short USD long EUR seems to have switched. Whether this is a prolonged correction, a change in trend or a pause in the overall Euro trend is difficult to ascertain, hence we look to the charts for suggestion.

Technically, EURUSD remains under great pressure. There are a combination of bearish signals that will cap upside probes.

-The close below 1.2092.

-The initial break lower through the 1.2200/1.2190 consolidation triangle support marks -a downside target of 1.1880, see chart.

-The weekly close below the 2017/2018 uptrend.

Prices are currently eroding the 200 mda at 1.2000, where we have presently stalled.

On Wednesday, EURUSD has opened up slightly higher, yet still capped by the 200 mda at 1.2015/20. We may see a small bounce from here, but this is expected to remain tepid while intraday stays below 1.2092. Risks to further downside remains high. Last week we highlighted that EURUSD was consolidating within a Bull flag pattern. We have no reason to doubt this as prices currently sit at the bottom of this structure at 1.2020/1.200. From here, we still see risk reward leaning towards being long. The +3% sell off from April 19th has met some demand just below 1.2000. Outright buying here is risky, considering we have cut through key support lines of 1.2155, the previous YtD low and 1.2090, the 2017 high. Furthermore, the bears will be quick to point out the present prices clearly trade below the 2017/18 supporting trendline. I believe we need to see a weekly close below 1.2090 pivot for confirmation of this.

Attempt intraday longs around 1.2095/1.2110 risking 1.2080. Initial upside targets await at 1.2150, the Feb low, and 1.2205, the 13 mda**.**

GBP

The pound was heavily sold last week by Carney's comments which raised doubts for a May hike. Sterling weakness was further compounded by weak GDP numbers and a stronger dollar. Last week expected some support at 1.3740/60 however weaker data resulted in this level been broken, pushing cable back onto the 2017/2018 supporting trendline.

GBPUSD has now eroded the strong 2018 uptrend at 1.3695/85 that historically has provided support. Failure here could see a slide towards the 200 mda at 1.3535 and 55 mwa at 1.3370.

At time of writing Cable still rotates around this trendline support, where I expect the haemorrhaging to pause supported by this multi-year TL, not ruling probes lower to 1.3650/70. This level also chimes with a sloping 2016/2018 and 200mda resistance lines for the dollar index. This week has seen liquidation of stale longs with the cross ploughing through the year to date low at 1.3712 March low. Below here at 1.3655/65 we expect some new demand.

This area is the 2017 high allowing for some consolidation. Intraday rallies will be capped at 1.3750/60. Above that, stronger resistance awaits at 1.3840 which guards 1.3990, the 55 mda. Looking at the candles session, we have had 10 day counts which may suggest some profit taking here.

For the sell to continue, markets need to see a close below 1.3660 pivot. We attach a low probability to this scenario, expecting at least a short term interim bounce from here.

We suggest buying at 1.3590/80 risking a close below the 200 mda at 1.3540/50 for a near term objective of 1.3760 and above that at 1.3930, the 38% Fibo of the April downswing.

USD

Dollar bulls will be encouraged by US yields, which, buoyed by the Federal Reserve's tightening monetary policy, are starting to reassert their influence over the currency. The correlation between rates on two-year Treasury notes and the dollar is firmly back in positive territory after turning negative in February and March for the first time in more than a year.

The USD continues its move higher having broken through the 91 pivot last week. The index now sits just below the 200 mda resistance area at 92.00. Failed probes over the past three sessions through this level have been resulted in a 0.50% retreat. The DXY's downtrend line from the 2016 highs too caps the advance just above 92.00. Above 92.00 next resistance sits at 90.70, the 50 wma. CFTC data showed an exit from some EUR and GBP positions supporting the current upswing, however at the present juncture both sit on decent support levels themselves. JPY positioning is still neutral with USDJPY being driven by long end US yields, nothing new there.

The dollar's recovery appears more broad based, now it has closed and re-opened above the 91.00 pivot this week. The DXY has seen gains against the majors with high beta and commodity currencies suffering most. Ex energy commodities are performing poorly, exacerbating AUD and NZD weakness.

We expect the dollar upswing to run into some headwinds in the middle of the week as prices meet decent technical resistance and with US economic event risk approaching. Technically the DXY made a YtD high on Tuesday at 92.25, the close above 91.00 drawing new bulls into the market.

Strong resistance is met here with the convergence of the 200 mda and 2016 sloping trend line which should cap prices over the short term. It is the downtrend line from the 2016 highs which may act as a large potential barrier for further dollar strength. Above 92.25 near term resistance is found at the 61% Fibo of the Nov Jan down move around 92.50, stronger resistance is at the 50 wma at 92.70. It is interesting at this level currencies such as GBP, EUR and AUD are all at the cusp of strong support when measured against the USD.

CHF

Recent comments from SNB Jordan underline their ongoing intention to press ahead with expansionary policy, warning that premature tightening of policy would risk undoing years of fighting the strong Franc, supporting the export-led economy. This underscores the Bank's commitment to keep policy loose while other central banks start to normalise their stances as the impact of the global financial crisis wanes and the global economy strengthened. In 2016, the Swiss economy improved, with capacity utilisation higher and unemployment lower. 4th Qrtr growth touched 1.9% YoY with inflation turning positive for the first time since 2011.

Governor Jorden also pointed out that the SNB will continue to pursue an expansionary monetary policy based on the negative interest rate it charges on sight. Jorden lastly said that inflation remains low and inflationary pressure is modest despite our expansionary monetary policy. "Tightening monetary conditions would be premature at this juncture".

USDCHF has broken higher through the 2016/2018 downtrend, stalling at a milder resistance line of 0.9970. This may hold prices over the short term. We remain bid while prices stay above the 200 mda support line at 0.9675/80 and the Feb uptrend at 0.9675. USDCHF has strengthened more than 8% bouncing off its Feb low of 0.9188. The upswing accelerated in April in tune with the broader dollar move. The cross now sits comfortably above the 2017 downtrend channel and 61% Fibo of the same move. Momentum indicators suggest a warning signal here as judged by the RSI overbought signal. Nevertheless, with the psychological 1.00 level set in its sights we expect prices to gravitate to this level before any notable weakness can occur. Stronger resistance is found at 1.0063, the Oct 2018 high.

Intraday we are still in the latest up channel with mild support at 0.9895/.9900. Support comes in at 0.9805, the 13 mda and 0.9770, the 24% Fibo of this year's surge. Long term outlook is for further strength.

AUD

The RBA left Rates unchanged this week at 1.5% for the 21st consecutive month, saying weak household spending and sluggish wages growth remain a concern for the economy. RBA governor Philip Lowe kept his comments on employment, inflation and the state of the housing market virtually unchanged from his April statement. It wasn't all negative though with Lowe expecting Australian growth to rise above 3% in 2018 and 2019.

The AUD has been suffering lately in the wake of lower Chinese demand, a potential Trade War, lower demand for base metals, the current RBA monetary policy stance and now a stronger dollar. Interest rate markets only discount a 25% chance of one 25 bps hike, too low in our opinion.

Late in March we suggested buying AUDUSD at 0.7650 with a tight stop as we were going against market consensus. 0.7650 marked a 76% Fibo of the same move, now completed at 0.7500.

We still favourable risk reward for buying the AUDUSD considering its position in the market.

Fundamentally, the RBA is less cautious on the economy. There is optimism in commodity markets and the probability of a trade war between the US and China has lessened.

Looking at the technical picture, AUDUSD sits on crucial support at 0.7500. The cross is holding the base well as marked by a short term channel. This is the late 2017 low. The candles suggest the cross is oversold with 11 consecutive down days, following by a 'piercing reversal pattern' on the daily candle sessions. Trendstall, a stop and reverse indicator is flashing a warning signal to bears and the RSI and MACD too indicate a market that looks like its suffering from selling fatigue. First resistance to the upside comes in at 0.7620/40, 38% Fibo of the April weakness, followed by 0.7645 the Mar April low and 76% Fibo. Risks to the upside argument are that prices remain firmly below the 2016/2018 uptrend at 0.7640 over the near term, and the 200 mda over the medium term.

Resistance above that awaits at 0.7735, the sloping trendline and the 76% Fibo of the April weakness. As noted the pivot 200mda line is 0.7800.

We recommend buying AUDUSD here at 0.7500/10 with a stop at 0.7460, just below the 0.7475, the 50% Fibo of the entire 2015/2018 trough peak move and YtD low of 0.7473. 240min charts suggest a bounce from here but prices need to close above 0.7545 for confirmation. Targets intraday are 0.7605, 0.7645 for medium targets at 0.7740 and 0.7790.

VIEWS FROM THE TRADING FLOOR

Equity

S&P rose 0.8% on the last week, with a stable volatility moving from 15.25 to 15.49. On the upside, automotive retail industry and health car REITs were up more than 8%. On the downside, distributors were down nearly 9% while copper was down 7%.

This week, in the US, the focus will be on the FOMC rate decision released today. The Fed Funds Futures show a 34% probability of a quarter-point hike at today's meeting which does not include a post-meeting press conference. The probability of a hike at the June meeting, which does include a press conference is still rising. The probability that the June hike will be a half point is now almost 31% and the probability that the June hike will be only a quarter point is now about 63%.

S&P 500: The index did not manage to break above its 2710 resistance and corrected toward its 2610 support. On the upside the next targets are 2710 before 2743-50 and 2850.

On the down side the main strong support area is 2610-2600 (the bottom of the uptrend initiated in February 2016. If it does not hold, then we can expect a correction toward 2532 before 2470 with a possible extension to 2350-2325.

Eurostoxx 50: The index extended its rally to 3553 its main resistance, the next one being 3643. Any correction will surely lead to 3525before 3450.

EQUITY

Developed countries

		Total return - 1 Week
SMI	↑	1.1%
Euro Stoxx 50	↑	2.2%
DAX	↑	2.0%
FTSE 100	↑	2.3%
S&P 500	↑	0.5%
Dow Jones	↑	0.0%
Nikkei 225	↑	0.9%

Developing countries

Russia/Micex	↑	2.3%
India/Nifty 50	↑	1.0%
China (HK)	↑	0.3%

↑ - Upward move ↓ - Downward move

FIXED INCOME

Developed countries

	2-year Yield	10-year Yield
USA	2.5%	3.0%
UK	0.8%	1.5%
Germany	-0.6%	0.6%
France	-0.5%	0.8%
Italy	-0.3%	1.8%
Spain	-0.4%	1.3%
Switzerland	-0.8%	0.1%

Developing countries

	2-year Yield	10-year Yield
Russia	3.8%	4.8%

COMMODITIES

		Total return - 1 Week
Crude Oil	↑	6.7%
Gold	↓	-2.6%

CALENDARS

Economic Events

Date of release	Domicile	Event	Period	Actual	Estimated
02 May 2018	US	FOMC Rate Decision	May	1.75%	1.75%
03 May 2018	US	Nonfarm Productivity	1Q	0.0%	0.9%
04 May 2018	Germany	Consumer Confidence	April	54.1	54.1
02 May 2018	Italy	Unemployment Rate	March	11.0%	10.9%

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