Weekly Update

C0 | EXTERNAL PUBLICATION

US dollar – what's behind the slide?


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The US dollar took a plunge this week, hitting 3-year lows against the euro, following a battle of words between US and eurozone policymakers. On Wednesday at the Davos summit, the US Treasury Secretary said dollar weakness was good for trade. Then, on Thursday, European Central Bank chairman Mario Draghi pointed out that the G7 had agreed in October not to talk down their currencies, a rebuke for Steve Mnuchin. And then Donald Trump arrived in Davos to say he was in favour of a strong dollar, which promptly rallied 1%.

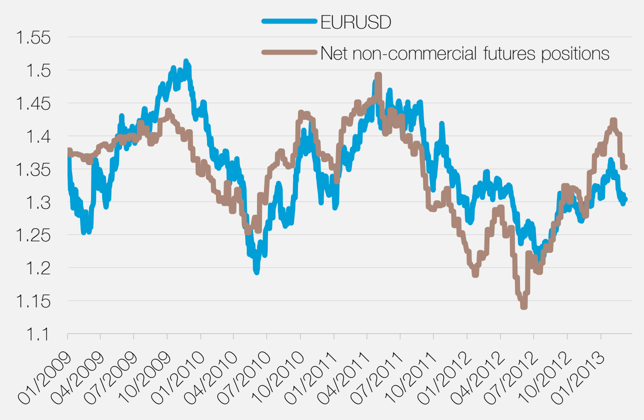
The greenback has been in a downtrend since late 2016 after Trump's election raised concerns of fiscal drift and broad-based deregulation in the US. The dollar index has lost 14% while the euro has rallied +19% against the dollar and sterling by +16%. However, this should be put into perspective.

1. The dollar has shed ground against higher-yielding emerging currencies as stronger global economic data has revived risk appetite.
2. The single currency has been bolstered by the eurozone recovery. The upward revision to 2017 growth data bodes well for 2018 and the resulting improvement in long-term inflation expectations has prompted the ECB to consider ending asset purchases in September 2018.
3. Sterling gains also reflect economic resilience in the UK thanks to stronger global growth.
4. The interest rate gap has not played in favour of the dollar. The yield curve's bear flattening – where short-term interest rates increase more than long-term yields – has weighed on the greenback. Yet, rate hike expectations have remained rather tame in the US as inflation has barely increased so far.
5. Long positioning on the euro has reached extremes, pushing the single currency up. US fiscal reform with lower taxes on repatriated capital should not be seen as a game changer. More than 90% of cash stored overseas by healthcare and IT companies is held in dollar-denominated bills and bonds, meaning that repatriations would impact rates more than currencies.

All this leads us to believe that the dollar could bounce back in the near term. With the market overly short USD, the recent slide looks a little overdone. A counter-trend rally could be triggered if the US Federal Reserve turns more hawkish or if ECB expectations are repriced. However, we remain very constructive on EUR/USD in the mid-term and stick to our targets of 1.25 for June and 1.30 for December 2018.

The market is now less long EUR, driving EUR/USD down

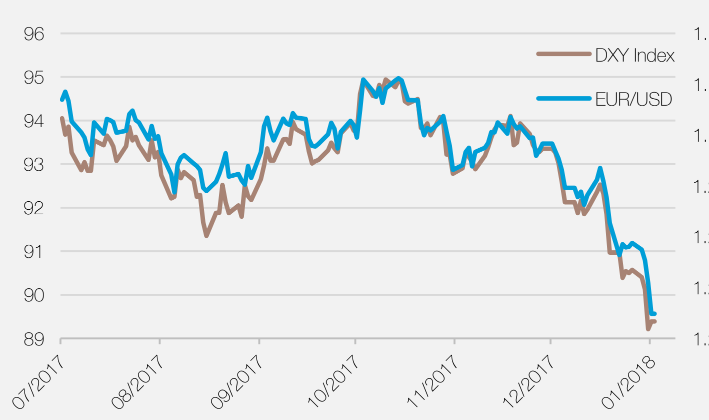
EUR/USD cross rate vs non-commercial positions on future contracts



Sources: SGPB, Bloomberg,26/01/2018

Dollar takes the plunge but could bounce back

EUR/USD cross rate (reverse scale) vs DXY dollar index



Sources: SGPB, Bloomberg,26/01/2018

This week and next

EUROZONE

- Eurozone consumer confidence improved further, reaching a 17-year high at 1.3 in December.
- Manufacturing PMI eased down from 62.2 to 61.1 in January, staying well-above the 50 threshold signalling economic expansion. Meanwhile, services PMI increased further.
- In January, the German IFO business climate index posted a high since November, supported by the "Current Situation" component, while "Expectations" eased down.
- In France, business confidence eroded in January, mainly in services and construction, while manufacturing sentiment improved.

Next week's key events		Per.	Prev.	Cons.
30 Jan	GDP QoQ	Q4 A	0.6%	0.6%
31 Jan	Unemployment rate	Dec	8.7%	8.7%
31 Jan	CPI YoY	Jan P	1.4%	1.2%

UNITED KINGDOM

- The UK unemployment rate has been stuck at a 4-decade low of 4.3% since July.
- In its first estimate, real GDP growth reached 0.5% in Q4 after 0.4% in Q3. However, on a year-on-year basis, UK growth slowed further to 1.5% in Q4. Over the whole 2017, real GDP grew 1.8%, marking a third year of deceleration.

Next week's key events		Per.	Prev.	Cons.
31 Jan	GfK consumer confidence	Jan	-13	-13
1 Feb	Manufacturing PMI	Jan	56.3	56.5

UNITED STATES

- Preliminary results show that manufacturing PMI improved further in January to 55.5 while services PMI reached its lowest level since August 2017 at 53.7.
- After a spike in October, the Conference Board's leading indicator rose 0.5% in November, mainly thanks to the ISM's "New Orders" component.
- Jobless claims edged up to 233K over the week of on January 19 but remained historically weak after a low at 216k on January 12.

Next week's key events		Per.	Prev.	Cons.
30 Jan	Core PCE (YoY)	Dec	1.5%	1.6%
31 Jan	FOMC Rate Decision	Jan	1.25%	1.25%
2 Feb	ISM Manufacturing	Jan	59.7	59.0

ASIA & EMERGING COUNTRIES

- Despite a supportive economic context, Japanese exports decelerated in December, from +16.2% YoY to +9.3%. However, in its first estimate for January, the manufacturing PMI rose further to 54.4.
- Japanese inflation accelerated from 0.6% YoY in November to 1.0% in December but remains below the Bank of Japan's 2% target.
- In China, industrial profits grew moderately in December for the third month in a row, reaching 10.8% YoY.

Next week's key events		Per.	Prev.	Cons.
30 Jan	Japan: Jobless rate	Dec	2.7%	2.7%
31 Jan	China: Manufacturing PMI	Jan	51.6	51.5

Sources: Datastream, Bloomberg, 26 January 2018, Note: YoY = year-on-year; QoQ = quarter-on-quarter; MoM = month-on-month, P = preliminary figure, A = advanced figure, F = final figure, seasonally adjusted, ECB = European Central Bank

Our 6-month targets

CURRENCIES & COMMODITIES

	Thursday close	6mth target
EUR/USD	1.22	1.25
GBP/USD	1.39	1.28
USD/RUB	56.5	60
AUD/USD	0.80	0.72
EUR/CHF	1.17	1.18
USD/CNY	6.42	7.1
USD/CAD	1.24	1.37
USD/JPY	111	118
Brent	$69.4	$55
Gold	$1329	$1225

No change to our 6-month targets this week.

Forecast figures are not a reliable indicator of future performance

Question time

Past performance should not been seen as a guarantee of future returns.

COUNTRY VIEW
Is Greece making any progress?

26 January 2018

Greece is on track to exit its eight-year "whatever it takes" bailout program.

Greece has experienced gradual economic recovery in recent quarters, thanks to the combined impact of global growth and financial support from European Union entities. Our economists expect growth to accelerate in 2018, reaching 2.4% versus 2.1% for the eurozone.

Economic sentiment has recovered steadily and confidence in the manufacturing sector has reached decade highs. Unemployment is falling gradually but still remains more than twice the euro zone average, especially among the younger segments. Consumer confidence has also improved steadily in the last twelve months, but retail sales still remain sluggish.

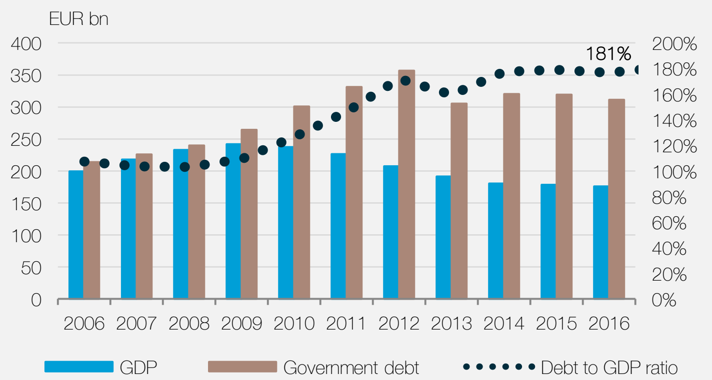
Greece has pushed ahead with the 113 reforms which were imposed by the International Monetary Fund (IMF) and European Union (EU), most recently with a package of labour, energy and fiscal reforms in January 2018. Our economists expect a primary budget surplus of 2.4% of GDP in 2017 (target: 1.75%) and 3.5% on average until 2020.

The third review of the bailout programme was concluded last Monday by eurozone finance ministers who approved a €6.7 billion cash injection in two tranches. This is the penultimate review of Greece's third bailout package from eurozone countries and the IMF. It bodes well for Greece, which should successfully complete its eight-year bailout program in August 2018. This progress means that Greece should soon be able to borrow money again from investors. Indeed, there is speculation that they may issue new bonds as soon as next month.

With no big debt redemptions due until mid-2019, Greece's short-term cash position looks solid. However, the size of the debt burden can only shrink gradually unless progress is made on sizeable debt relief.

The size of the debt burden can only shrink gradually unless progress is made on sizeable debt relief

Annual GDP growth (%), government debt (bn €) and debt-to-GDP ratio



Sources: Societe Generale Private Banking, Bloomberg, Bloomberg, up to 2016.

The last week has brought two items of good news for Greece. First, the vote by Germany's SPD to authorize talks with Chancellor Merkel on a new grand coalition opens the door to a less hard-line approach to dealing with Greece's dilemma. Second, the new Eurogroup president Mario Centeno indicated that technical talks on debt relief can now be scheduled.

The road ahead remains long. Major issues such as the non-performing loans – which constrain Greek banks' ability to lend – are still on the table. But the skies over Athens are beginning to clear.

COUNTRY VIEW
Looser FX regime in Morocco – what impact?

26 January 2018

On January 15, Morocco widened the dirham's fluctuation band versus a reference basket consisting of the euro and the dollar. The band was widened from ±0.3% to ±2.5%.

This long-awaited measure had been recommended by the International Monetary Fund (IMF) in order to enhance capital flows and open the economy further to the world. The decision was welcome by the market and the currency has appreciated versus the dollar and depreciated against the euro since January 15.

The measure aims at:

1. Reducing the balance of payment deficit;
2. Helping the financial sector grow thanks to greater capital mobility.
3. Sending a positive signal to foreign investors (China now represents 10% of imports versus 5% ten years ago).

All this will allow the central bank to keep the dirham under tight control and retain a rather high level of currency reserves. These last few months, the Moroccan central bank and IMF have agreed that the currency regime should be more fundamentally-driven.

A strong economy, a cautious fiscal policy, tame price pressure and the rise in foreign direct investment should help to limit the depreciation in the Moroccan dirham versus the euro. However, in the medium term, the euro is likely to strengthen against most currencies thanks to the eurozone economic recovery and to the currency's undervaluation.

Market performance

Past performance should not been seen as a guarantee of future returns.

Interest rates

Interest rates	Last	1wk		3mth	YTD	12mth
EONIA (EUR)	-37 bp	-1 bp	→	-1 bp	-2 bp	-2 bp
3mth Euribor (EUR)	-33 bp	0 bp	→	0 bp	0 bp	0 bp
3mth Libor (USD)	174 bp	2 bp	↑	38 bp	5 bp	71 bp
3mth Libor (GBP)	52 bp	0 bp	→	14 bp	0 bp	17 bp
10-year US Treasury bond	261 bp	8 bp	↑	27 bp	20 bp	22 bp
10-year German bond	51 bp	-2 bp	↓	11 bp	8 bp	16 bp
10-year French bond	72 bp	-2 bp	↓	7 bp	6 bp	-10 bp
10-year UK bond	137 bp	2 bp	↑	2 bp	15 bp	4 bp

Credit

Credit	1wk		3mth	YTD	12mth
BAML EURO Corp. IG	0.2%	↑	0.0 %	0.0 %	2.7 %
BAML EURO Corp HY	0.2%	↑	0.6 %	0.6 %	6.7 %
BAML GBP Corp IG	0.1%	↑	1.4 %	-0.1 %	5.5 %
BAML US IG	-0.3%	↓	0.1 %	-0.7 %	5.1 %
BAML US HY	0.0%	→	0.7 %	0.7 %	7.0 %
JPM Global EM Sov. Plus	0.3%	↑	1.2 %	0.5 %	10.4 %

Exchange rates

Exchange rates	Last	1wk		3mth	YTD	12mth
EUR/USD	1.22	1.7 %	↑	3.8 %	1.9 %	15.1%
EUR/CHF	1.17	-0.1 %	→	1.4 %	0.3 %	9.6%
GBP/USD	1.39	2.6 %	↑	5.2 %	2.9 %	13.3%
USD/JPY	111	-0.1 %	↓	-1.6 %	-1.4 %	-3.1%
USD/BRL	3.21	-0.3 %	↓	1.1 %	-3.2 %	-0.8%
USD/CNY	6.42	-1.2 %	↓	-3.1 %	-1.3 %	-6.1%
USD/RUB	56.5	0.1 %	→	-1.7 %	-2.0 %	-5.1%

Government bonds*

Government bonds*	1wk		3mth	YTD	12mth
United States (3-7yr)	-0.4 %	↓	-1.2 %	-0.8 %	0.3 %
United Kingdom (3-7yr)	-0.2 %	↓	-0.3 %	-0.6 %	-0.1 %
Germany (3-7yr)	0.0 %	→	-1.0 %	-0.4 %	-1.2 %
Japan (3-7yr)	0.0 %	→	0.0 %	-0.1 %	-0.3 %

Equities*

Equities*	Last	1wk		3mth	YTD	12mth
MSCI AC World	537	1.3 %	↑	8.7 %	4.7 %	27.6 %
Eurostoxx 50	3 621	0.7 %	↑	0.3 %	3.4 %	13.6 %
DAX	13 281	0.6 %	↑	1.8 %	2.8 %	14.5 %
CAC 40	5 495	0.1 %	↑	2.4 %	3.5 %	16.8 %
S&P 500	2 798	1.1 %	↑	9.8 %	4.7 %	25.6 %
FTSE 100	7 701	-0.8 %	↓	2.7 %	0.2 %	10.6 %
SMI	9 452	-0.5 %	↓	1.5 %	0.8 %	17.5 %
Topix	1 877	-0.6 %	↓	9.0 %	3.3 %	26.6 %
IBOV Brazil	80 963	2.0 %	↑	5.7 %	6.0 %	26.2 %
MICEX Russia *	2 297	2.3 %	↑	9.7 %	8.9 %	5.9 %
MSCI EM	1 228	2.6 %	↑	9.3 %	6.1 %	40.2 %
SENSEX 30 India	35 260	2.2 %	↑	8.4 %	4.3 %	31.0 %
Hang Seng (H-K)	32 122	3.2 %	↑	12.0 %	7.4 %	44.5 %
Shanghaï Composite	3 475	1.4 %	↑	2.7 %	5.1 %	11.6 %

Commodities

Commodities	Last	1wk		3mth	YTD	12mth
Brent	$69	-0.8 %	↓	19.9 %	4.1 %	25.5 %
Gold	$1 329	0.6 %	↑	3.8 %	2.0 %	9.4 %
Silver	$17.0	0.3 %	↑	0.1 %	0.1 %	-1.5 %

Source: Datastream, on 25 January 2018. 1wk = 1-week change, 3mth = 3-month change, 12mth = 12-month change, YTD = year-to-date change, YoY = year-on-year change, BAML = Bank of America Merrill Lynch, JPM = JP Morgan, IG = Investment Grade, EM = emerging markets. * Price return for MICEX equity index. Equities; total return in local currency. Government bonds = 3-7 year returns. Figures are rounded.

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