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CURRENCIES & MORE OUR INSIGHT INTO THE WORLD'S LARGEST MARKET

Krone: The Conservative-led government from Prime Minister Erna Solberg won a second term
Dollar: With FOMC members in the black-out period, market participants are focusing on macro data
Pound: Inflation is likely to have increased again in August while wage growth remains subdued

Krone: The two ladies are confirmed again

Yesterday, Norwegians headed for the polls to elect their Storting, the Norwegian Parliament. The election was turning into a real race to the finish line, with the two biggest parties – Arbeiderpartiet (Labor Party) and Høyre (Conservative Party) – running neck and neck.

Erna Solberg and Siv Jensen



Source: Getty Images

In the end, incumbent Prime Minister Erna Solberg's Høyre Party in coalition with Siv Jensen's Fremskrittspartiet (Progress Party) and two other small parties managed to defend their government. Together, they secured 88 of the 169-seat Storting. The opposition Arbeiderpartiet got 49 seats or 28 percent of the votes. At the peak, Arbeiderpartiet led the opinion polls with over 40 percent but with spending an unprecedented amount to prop up Norway's economy, Solberg and her coalition succeeded to become the first center-right Government since World War II to serve two full consecutive terms. Solberg's first term as Prime Minister was clearly not easy. Soon after assuming office in 2013, Norway's economy was hit hard

by a sharp drop in oil prices. More than 50'000 jobs were wiped out in the oil industry alone. The unemployment rate rose from 2.4 percent to 3.4 percent at the beginning of 2016 when oil prices reached their lows around \$ 30 per barrel. Recovering oil prices clearly helped, but also that her government responded with tax cuts and investments in infrastructure, covered mostly by the first ever withdrawals from Norway's \$ 1 trillion Wealth Fund. These measures have worked as the unemployment rate dropped to 2.7 percent and GDP growth accelerated again. These developments have made life harder for the Arbeiderpartiet, which spent much of the election campaign trying to criticize the government's economic credentials. Party Leader Jonas Gahr Støre repeatedly said that the government has spent too much oil money, and they have spent it in the wrong way. The electorate obviously has seen it differently, namely that the purpose of the Wealth Fund is precisely to be here for rainy days.

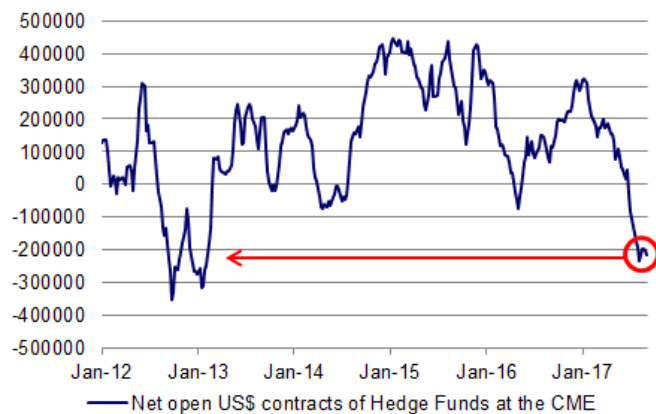
Conclusion: The outcome of yesterday's elections bodes well for the Krone.

Dollar: The roadmap until the FOMC meeting

The Dollar continues to be tested by speculators and investors. As we entered the black-out period ahead of the FOMC meeting, there will be no comments from Fed Officials until 20 September. Consequently, FX markets will focus on news out of D.C. and macro-economic data released ahead of the FOMC meeting. The data calendar until then provides information on inflation (PPI on the 13th, CPI on the 14th), consumption (retail sales on the 15th), output (industrial production on the 15th), sentiment (University of Michigan Sentiment Index on the 15th), trade and foreign investments (current account balance on the 19th). The market's focus will particularly be on inflation, given the decline since the beginning of

this year. Compared to a year earlier, inflation has slowed substantially from 2.7 percent (headline CPI) and 2.3 percent (core CPI) to 1.7 as of July. They can ebb and flow in response to the business cycle, but the upside is clearly not as strong as it once was. Several Fed officials have argued prior to the black-out period that interest rates are close to neutral, implying little need for further rate hikes. Currently, rates markets are pricing in only 20 basis points of cumulative rate hikes between now and the end of 2018. Also, positioning remains skeptical on the Dollar, according to net open futures at the Chicago Mercantile Exchange. Hedge funds and other large speculators are net short 215'000 contracts against the 8 currencies traded at the CME. This is largest short since 2012/2013 (see chart below). Is this a reversal pattern? Not necessarily, as the Dollar Index hardly moved during the period between September 2012 and February 2013 when net short went from -300'000 to -100'000 and back to -300'000 again.

Net Dollar positioning at the CME



Source: Bloomberg Finance L.P., Julius Bär

Conclusion: We still do not yet see a catalyst for the Dollar turning around in the next few weeks.

QUICK NEWS HEADLINES (time in CEST)

The following two headlines might have an impact on currency markets today:

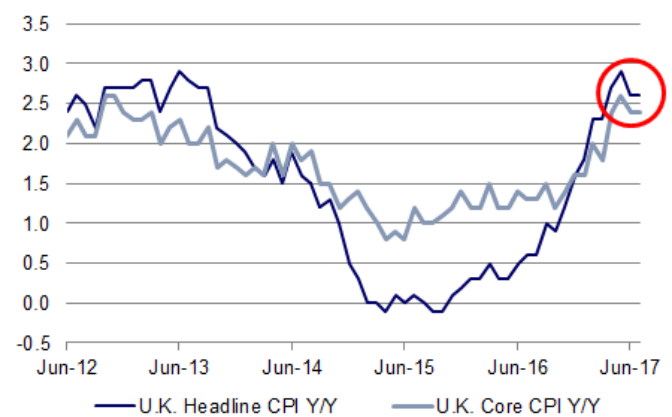
- Sweden: Headline CPI and underlying inflation are expected to have increased 2.2% in August y/y (09:30).
- Brazil: Retail sales are expected to have risen 3.2% in July y/y (14:00).

Pound: Inflation still (too) high

The Pound likely remains buffeted by everything from Brexit to the BoE. Last night, Prime Minister Theresa May enjoyed a victory. The House of Commons passed a bill

designed to allow her government to copy E.U. law and enshrine it into domestic statute. Later this morning, the ONS will release inflation prints for August. Headline CPI is expected to have risen 2.8 percent from a year earlier while core inflation is expected at 2½ percent. The two have moderated to 2.6 and 2.4 percent in June and July (see chart below). As wage growth continues to lag CPI increases, this will further eat into consumer spending and therefore weigh on GDP.

Headline and core CPI are stalling at high levels



Source: Bloomberg Finance L.P., Julius Bär

Conclusion: We still recommend staying short the Pound.

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