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Impact of December Fed hike

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- It seems increasingly likely that the Fed will start a slow rate hike cycle in December...
- ...resulting in a stronger US dollar versus the euro, yen and precious metals
- We have kept our EM and commodity FX forecasts largely unchanged

Adjusting our Fed rate hike view

Following the stronger-than-expected US employment report and hawkish commentary from Fed members, we have put a 25bp rate hike for December back in our base scenario. This rate hike will probably be accompanied with a dovish statement to contain expectations of further early action and hence limit the impact of the rate increase. For 2015, financial markets have priced in a 66% probability of a rate hike at the December meeting (see graph below). In 2016 we expect the Fed to continue raising interest rates by a total of 75bp with the first of those to come in June. This is around 30bp above market expectations (if calculated from the mid of the range) (see Global Daily Insight of 12 November 2015).

Probability Fed funds range 0.25-0.50% December 2015



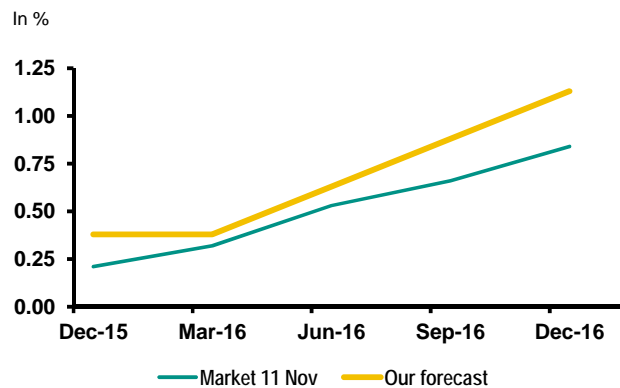
Source: Bloomberg

We lower EUR/USD for 2015 and 2016...

The adjustment in our Fed rate hike call today has prompted us to upgrade the US dollar view versus the euro, the Japanese yen, Singapore dollar and precious metals. We now expect a test in EUR/USD of the March low just below 1.05 before the end of the year.

Therefore, our new year-end forecast is 1.05. The dovish statement following the December rate hike will likely result in some stabilization in EUR/USD at the start of 2016. We have also lowered our EUR/USD forecast for the end of 2016, mainly because of more monetary policy divergence on either side of the Atlantic, with the ECB likely to continue QE through the year. We have more Fed rate hikes than financial markets currently anticipate (see graph below). We expect financial markets to catch up with our view in the course of next year. We expect parity in EUR/USD to be reached in March 2016 and 0.95 in June 2016. As a result, we have put EUR/USD back in our list of high conviction shorts.

Expectations & our forecast of mid-point Fed funds rate



Source: Bloomberg

...and we also lower our yen and Singapore dollar forecasts

We are now slightly more bearish on the Japanese yen and the Singapore dollar given their high sensitivity to short-term yields in the US. The recent strong US employment report and upward adjustment in expectations about a possible Fed rate hike in December financial markets have already pushed USD/JPY to 123 and USD/SGD above 1.42. If the Fed delivers this rate hike in December, it is likely that USD/JPY will rally to 125 and USD/SGD to 1.43.

Our bearish view on the yen is mainly the result of the divergence in monetary policy. In addition domestic investors are likely to position for overseas assets during periods of JPY strength. Indeed domestic life insurers have indicated their bias to increase overseas assets on an unhedged currency basis. We maintain long USD/JPY in our conviction list.

But leave our EM FX and Commodity FX largely unchanged

We have kept our EM and commodity FX forecasts largely unchanged. In general the sharp weakness in emerging market currencies will likely result in positive developments in the trade balances of these countries. In addition, a stabilisation and slight upward momentum in commodity prices should take away some of the negative sentiment in currencies of commodity exporters. Moreover, the slowdown in China will likely be less severe than financial markets currently anticipated. Last but not least, we expect investor sentiment to be positive resulting in investors searching for global growth exposure and higher-yielding currencies. This is positive for

currencies where central banks have stopped their easing cycle and the next step is to tighten.

However, there are clear negatives for these currencies. Most of them remain vulnerable as interest rates in the US rise. Other headwinds could be the domestic political situation, the economy and possible downgrades. If we take all these factors into account the overall picture is mixed. We see some recovery in Latin American currencies, Russian ruble, South African rand because of stabilisation of commodity prices and some improvement on the domestic front. We remain bearish on Asian currencies as a weaker Chinese yuan, euro and Japanese yen will remain headwinds for Asian exports and monetary policy easing in Asia weighs.

We remain bearish on commodity currencies like the Australian, New Zealand and Canadian dollar mainly because of monetary policy divergence and the continued drag on the economy of the correction in commodity markets. Our change in Fed call may result in less dovish central banks in Australia, New Zealand and Canada. Therefore the impact will be muted.

ABN AMRO major currency forecasts

Changes in red/bold

| | 12-Nov | Q4 2015 | Q1 2016 | Q2 2016 | Q3 2016 | Q4 2016 |
|---------|--------|-------------|-------------|-------------|-------------|-------------|
| EUR/USD | 1.0733 | 1.05 | 1.00 | 0.95 | 0.95 | 0.95 |
| USD/JPY | 122.96 | 125 | 127 | 130 | 133 | 135 |
| EUR/JPY | 131.98 | 131 | 127 | 124 | 126 | 128 |
| GBP/USD | 1.5191 | 1.50 | 1.43 | 1.36 | 1.38 | 1.40 |
| EUR/GBP | 0.7066 | 0.70 | 0.70 | 0.70 | 0.69 | 0.68 |
| USD/CHF | 1.0041 | 1.05 | 1.10 | 1.18 | 1.20 | 1.21 |
| EUR/CHF | 1.0777 | 1.10 | 1.10 | 1.12 | 1.14 | 1.15 |
| AUD/USD | 0.7111 | 0.70 | 0.68 | 0.66 | 0.64 | 0.62 |
| NZD/USD | 0.6524 | 0.64 | 0.62 | 0.6 | 0.58 | 0.58 |
| USD/CAD | 1.3305 | 1.33 | 1.35 | 1.37 | 1.39 | 1.41 |
| EUR/SEK | 9.2970 | 9.50 | 9.50 | 9.50 | 9.50 | 9.50 |
| EUR/NOK | 9.3301 | 9.50 | 9.25 | 9.00 | 8.75 | 8.50 |
| EUR/DKK | 7.4602 | 7.46 | 7.46 | 7.46 | 7.46 | 7.46 |

Source: ABN AMRO Group Economics

ABN AMRO emerging market currency forecasts

Changes in red/bold

| | 12-Nov | Q4 2015 | Q1 2016 | Q2 2016 | Q3 2016 | Q4 2016 |
|--------------------|--------|-------------|-------------|-------------|-------------|-------------|
| USD/CNY (onshore) | 6.37 | 6.40 | 6.45 | 6.50 | 6.55 | 6.55 |
| USD/CNH (offshore) | 6.40 | 6.40 | 6.47 | 6.53 | 6.57 | 6.57 |
| USD/INR | 66.3 | 66 | 66 | 67 | 67 | 67 |
| USD/KRW | 1,158 | 1,190 | 1,200 | 1,220 | 1,230 | 1,240 |
| USD/SGD | 1.42 | 1.43 | 1.45 | 1.47 | 1.48 | 1.50 |
| USD/THB | 35.90 | 36.80 | 37.00 | 37.20 | 37.50 | 38.00 |
| USD/TWD | 32.72 | 33.00 | 33.50 | 33.70 | 33.80 | 34.00 |
| USD/IDR | 13,597 | 14,300 | 14,500 | 14,800 | 14,900 | 15,000 |
| USD/RUB | 66 | 60 | 60 | 55 | 55 | 55 |
| USD/TRY | 2.88 | 3.10 | 3.05 | 3.00 | 2.95 | 2.90 |
| USD/ZAR | 14.29 | 14.00 | 13.80 | 13.60 | 13.40 | 13.20 |
| EUR/PLN | 4.23 | 4.15 | 4.10 | 4.05 | 4.00 | 4.00 |
| EUR/CZK | 27.50 | 27.50 | 27.40 | 27.25 | 27.00 | 26.75 |
| EUR/HUF | 312 | 315 | 315 | 310 | 310 | 310 |
| USD/BRL | 3.82 | 4.00 | 3.90 | 3.85 | 3.80 | 3.75 |
| USD/MXN | 16.81 | 17.00 | 16.75 | 16.50 | 16.25 | 16.00 |
| USD/CLP | 703 | 700 | 690 | 680 | 670 | 660 |

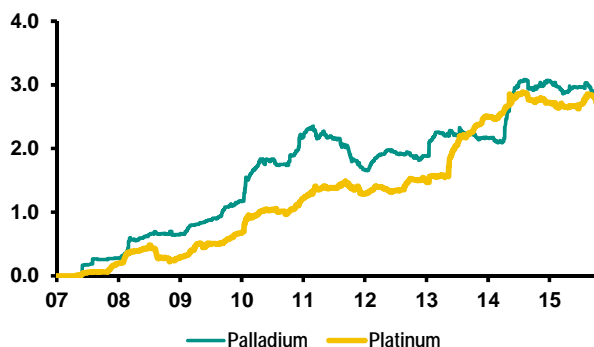
Source: ABN AMRO Group Economics

More negative on gold prices...

In our precious metals weeklies, we focussed on the interrelated driving forces for gold prices such as the direction in the US dollar and expectations about monetary policy. The Fed has been a key driver of precious metals over the recent weeks and this will likely continue in the weeks and months ahead. Our above-consensus Fed call should push gold prices towards USD 1,000 per ounce this year and USD 900 per ounce in 2016 mainly because of investor position liquidation. We remain optimistic on gold jewellery demand and this will likely reduce the downside somewhat.

ETF liquidation under way

Total ETF positions in million troy ounces



Source: Bloomberg, ABN AMRO Group Economics

...as well as on other precious metals

The upward adjustment in Fed rate hike expectations and the higher US dollar have also been negative for other precious metals. A shift in investor sentiment is currently unfolding resulting in liquidation of total ETF positions in platinum and palladium. The widening of the emission scandal has also had its negative impact on palladium and platinum prices. Platinum prices broke below previous low set in October reinforcing the negative price outlook. In the current negative sentiment platinum prices could drop as low as USD 800 per ounce (-9%) and palladium prices as low as USD 530 per ounce (-6%) before the end of the year. Silver prices will likely continue to track gold prices. For 2016, we expect a weakness in gold prices to continue and an outperformance of the cyclical precious metals over gold.

ABN AMRO precious metals forecasts

Changes in red/bold

| End period | 12-Nov | Close 14 | Mar-15 | Jun-15 | Sep-15 | Dec-15 | Mar-16 | Jun-16 | Sep-16 | Dec-16 |
|------------|--------|----------|--------|--------|--------|--------------|--------------|------------|------------|------------|
| Gold | 1,082 | 1,185 | 1,184 | 1,172 | 1,112 | 1,000 | 1,000 | 950 | 950 | 900 |
| Silver | 14.3 | 15.7 | 16.6 | 15.7 | 14.5 | 13.5 | 13.5 | 14.0 | 14.5 | 15.0 |
| Platinum | 877 | 1,216 | 1,141 | 1,081 | 910 | 800 | 800 | 850 | 900 | 950 |
| Palladium | 565 | 798 | 736 | 674 | 652 | 530 | 530 | 550 | 600 | 650 |

| Average | Q1 15 | Q2 15 | Q3 15 | Q4 15 | 2015 | Q1 16 | Q2 16 | Q3 16 | Q4 16 | 2016 |
|-----------|-------|-------|-------|--------------|--------------|--------------|-------------|------------|------------|-------------|
| Gold | 1,218 | 1,193 | 1,126 | 1,106 | 1,165 | 1,000 | 975 | 950 | 925 | 963 |
| Silver | 16.7 | 16.4 | 15.0 | 14.8 | 15.9 | 13.5 | 13.8 | 14.3 | 14.8 | 14.1 |
| Platinum | 1,194 | 1,129 | 993 | 905 | 1,075 | 800 | 825 | 875 | 925 | 856 |
| Palladium | 786 | 759 | 618 | 651 | 700 | 530 | 540 | 575 | 625 | 568 |

Source: ABN AMRO Group Economics

Find out more about Group Economics at: <https://insights.abnamro.nl/en/>

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