FXTM

QUARTERLY **MARKET** FORECAST

2018

Q1

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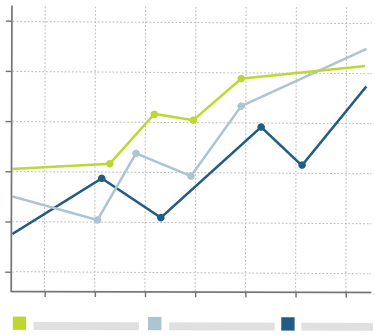
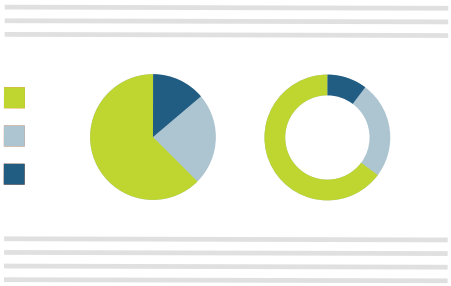
2018 will be the year of change

Written by Hussein Sayed,
Chief Market Strategist at FXTM

2017 has been a very kind year for bullish equity investors. Nearly all equity markets across the world saw substantial gains, and most equity indices grew by double digits. Synchronized global expansion, strong corporate earnings, loose monetary policies, and of course, U.S. tax reforms, all compensated risk takers.

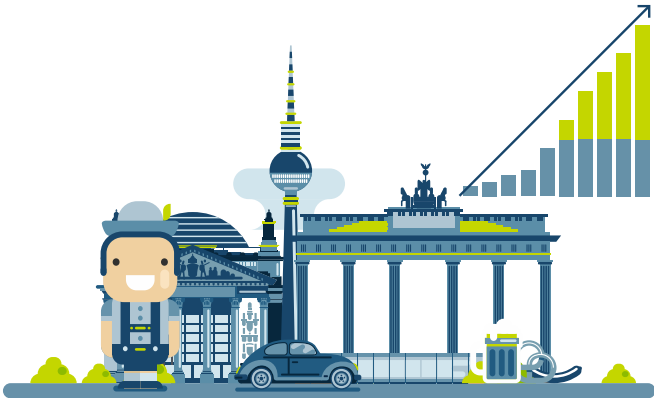


There were plenty of disruptive factors in play that could have influenced the bears, but they appeared to have been blinkered. The political drama in Washington, Brexit uncertainty, the rise of protectionism, and geopolitical risks were all ignored. Instead, volatility dropped to an all-time low of 8.56 in November, and the Dow Jones industrial average achieved a record number of all-time highs. 2017 may be simply labelled as the most peaceful and rewarding market in decades.



While we continue to believe global growth will remain healthy in 2018, several catalysts are likely to bring the bears back in town.

Central banks have been investors' best friends since the global financial crisis. Quantitative easing programs boosted growth in major economies, reduced risk premium in many asset classes, and sent bond prices to unprecedented levels -with $11 trillion of sovereign and company debt in negative yields. Now with all major central banks shifting towards tightening monetary policies, downturn risks seem high, especially towards the third quarter of 2018. The reversal of QE will sap liquidity in fixed income markets, so any policy mistake at this stage may shock investors in a similar manner to the 2013 taper tantrum.



Despite the political turbulence in Europe, most countries within the Euro area enjoyed robust economic growth in 2017. We expect this momentum to continue next year, driven by the revival in the global economy, positive consumer sentiment and relatively easy monetary policy. However, Italy's election, Germany's political drama, and Brexit negotiations will continue to present tail risks which investors should be aware of.

01

EURUSD:

Buoyed by Europe's improving macro fundamentals

Written by Lukman Otunuga, Research Analyst at FXTM

The Euro voyaged within a wide range against the Dollar during the final quarter of 2017 as investors tussled with the various market themes driving the currency pair.

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An unwelcome return of political uncertainty in Europe following Catalonia's illegal independence referendum, swiftly dented investor attraction towards the Euro during early October. Although the currency managed stay afloat during political uncertainty in Spain, this was short lived after German Chancellor Angela Merkel failed to form a new government in November. With anxiety brewing ahead of the Italian General election this year, polls show the Eurosceptic party Five Star Movement (5S) gaining lead, this means the Euro could face some headwinds down the road. While political risk has the ability to entice bears in the short term, Europe's steadily improving macro-economic landscape is likely to cushion the Euro's

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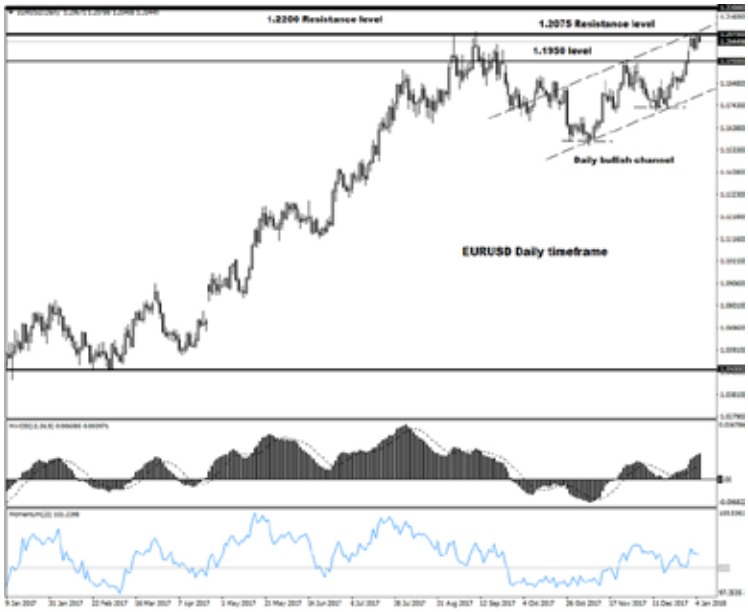

02

GBPUSD:

Bulls banking on Brexit breakthrough

Written by Lukman Otunuga, Research Analyst at FXTM

The story around **Sterling's aggressively volatile price action** during the final trading quarter of 2017 revolved around political risk, stalled Brexit negotiations and **growing uncertainty over the outlook of the UK economy**.

Although the British Pound surprisingly appreciated near the end of Q4, there is a strong suspicion that this had nothing to do with a change of sentiment towards the British Pound but rather- broad-based Dollar weakness. With Brexit uncertainty still a recurrent market theme and the Budget Responsibility (OBR) revising down growth forecasts for the next five years, the Pound is still at threat of depreciating. While a vulnerable Dollar remains a key culprit behind the GBPUSD's impressive appreciation, another factor could be some cautious optimism over Brexit negotiations reaching another breakthrough in 2018.

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04

AUDUSD:

Are Aussie bulls relying on Dollar weakness?

Written by Lukman Otunuga, Research Analyst at FXTM

The Australian Dollar bounced back to life during the final trading weeks of Q4, amid broad-based U.S Dollar weakness. Aussie bulls were inspired further, thanks to improving confidence over the Chinese economy and rising commodity prices which elevated the currency pair higher.

While the Australian Dollars high yielding status is likely to compliment the upside gains, bulls could still face some headwinds down the road. With markets somewhat downbeat about the Australian Dollar amid soft macro-economic conditions at home, the current optimism around the AUDUSD's appreciation could be built on weak foundations.

As we head into Q1, monetary policy in the States and at home, the value of the Dollar and commodity prices are likely factors that will impact the Australian Dollar's performance. The Reserve Bank of Australia has recently expressed confidence in inflation and unemployment, while dropping hints of raising interest rates. With concerns still present over low inflation, weak wage growth and elevated debt levels, there is scepticism over the central bank's

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GOLD

Shines into the New Year

Written by Lukman Otunuga, Research Analyst at FXTM

The combination of escalating geopolitical tensions, elevated global equity markets, and Dollar volatility transformed Gold into a battle ground for bulls and bears during the most part of Q4. Political uncertainty, worldwide tensions, and Dollar weakness were the catalysts for higher prices, while optimism over the global economy and prospects of US tax cuts, offset gains. With the yellow metal sprinting to a three month high on the last trading day of 2017 despite Congress passing Trump's mammoth $1.5 trillion tax overhaul, bulls could be back in town.

As we head into the first trading quarter of 2018, Gold has already started on a strong bullish note, with prices punching above $1320 as of writing. Although a heavily vulnerable Dollar is the likely cause behind Gold's aggressive appreciation, another factor could be geopolitical unrest in Iran stimulating the flight to safety. Investors should keep in mind that there are numerous other geopolitical risks which could ensure that Gold remains supported. These risks range from continued sabre-rattling between the US and North Korea, political drama in Europe and Brexit uncertainty. Another key factor which has the ability to impact Gold outlook is the Federal Reserve's monetary policy. Although sentiment remains bullish towards the US economy amid improving macro fundamentals, concerns still linger over the stubbornly low levels of inflation. With low inflation concerns clouding the prospects of higher rates, there are doubts over the Federal Reserve's ability

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