Trade Idea – Foreign Exchange

EUR/SEK uptrend to fade

2\textsuperscript{nd} September 2016

Brexit has kept SEK pressured

- Sweden’s strong trading and investment links with the UK have made the SEK vulnerable to weakness following the UK’s surprise decision to leave the EU in June (see Uncertainty to pressure the Krona). Indeed, between the vote and the start of August the SEK fell approximately 3.1% on a trade weighted basis as concerns over the impact of Brexit created downside for the currency. More recently however, this trend has shown some early signs of reversing. Strong economic reports out of the UK and Sweden have pointed to a less severe initial reaction to Brexit than many had anticipated, providing the SEK with some support over the past month. In the absence of any major decisions regarding the future of UK-EU relations, we believe that the SEK looks poised to move higher in the short term, particularly against the Euro. The EUR/SEK is currently trading near the top of its recent range and should it fall through some key support levels the pair has potential to move lower in the coming months.

\begin{figure}
\centering
\includegraphics[width=\textwidth]{figure1.png}
\caption{Swedish inflation climbs}
\label{fig:inflation}
\end{figure}

\textbf{Braced for impact}

- Stronger than expected July retail sales and consumer confidence data from the UK have all given some weight to the belief that the initial impact of Brexit was previously overestimated. It is indeed true that the market has managed the volatility of Brexit relatively smoothly, but the outcome of the vote has yet to really take shape. The true impact of Brexit will unlikely be felt until Theresa May actually invokes Article 50 and negotiations with the EU begin. Until then, strong data from the UK has potential to undermine Brexit concerns and provide the SEK with support.

- The last Riksbank meeting in July was relatively uneventful. The bank stated a willingness to do more (further rate cuts or asset purchase) should it be warranted, but for now appeared happy with inflation progressing nicely towards its 2\% target (see Figure 1). The Executive Board appeared to be taking a reactive approach to Brexit and will likely keep monetary policy unchanged until the actual economic impact of the vote materialises. This means, providing there are no other shocks, the SEK is unlikely to face pressure from a shift to more accommodative monetary measures any time soon. The next monetary policy meeting is scheduled to take place on the 7\textsuperscript{th} September.

*All figures quoted are sourced from Bloomberg unless stated otherwise.
**At a turning point**

- Since the end of 2014 the EUR/SEK has been trading in the broad 9.1-9.6 range, rarely being able to sustainably close higher than 9.6 without subsequently falling considerably lower (SEK strengthening). Currently, the EUR/SEK is at 9.55 and is looking increasingly overbought at a time when market positioning towards the Euro is turning increasingly bearish. Current levels appear an attractive point through which to acquire short exposure to the EUR/SEK currency pair (long SEK exposure) and benefit from near term SEK appreciation. Should the pair penetrate its own 50 daily moving average of approximately 9.47, a level which has recently been a short term support level, then we could see the pair fall considerably lower.

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