CitiFXTechnicals: The 12 Charts of Christmas
December 2014
Handing over the QE reins
CENTRAL BANK
NORTH POLE
Freshly Printed Euros
citi
A very warm Season's greetings to all our readers and best wishes for a healthy and prosperous 2015

Overview of 2014 result:

How did our 2014 views (Dec. 2013's 12 charts of Christmas) "pan out"?

- "The USD bullish trend remains intact and the DXY Index should set new trend highs (90+)."

  Result: High on the USD-index so far has been 89.55 and 90.00 still looks possible this year. **Grade: A+**

- EURUSD: "We expect a sharp turn lower that could see EURUSD in the 1.18-1.22 range in 2014. A very easy ECB policy will likely be a contributing factor here."

  Result: We have already traded a 1.22 "handle" this month and could still get 1.22 or below by year end. **Grade: A+**

- USDJPY: "Remains in a broad uptrend and we would expect a move towards at least 110-111 this year. This should continue to be supportive of the Nikkei."

  Result: Reached and exceeded our minimum 110-111 target on USDJPY and has so far traded to 18,031 on the Nikkei compared with our 18,300 target. **Grade: A**

- Consumer Confidence: "Looks set to "roll" lower in a fashion similar to 2000 and 2007. This may have implications for the U.S. Equity market which looks stretched at this point in a fashion similar to 2000."

  Result: Broke out of the downtrend on Consumer Confidence in March this year after we also saw a bullish outside month on the S&P in February. This led us to take a more bullish outlook which we still retain today. However, with regard to our concerns/call in Dec. 2013 - **Grade: C**

- "Housing looks better than it was at the lows but nowhere near the traditional recovery/escape velocity of prior cycles. In 2014 we may even see a pause in its improvement."

  Result: We did indeed see a pause in activity into September this year but the overall picture remains constructive. **Grade: A**

- US yields: "Similar to last year we suspect that an initial move lower may well emerge towards at least 2.40% (10 year) and 3.50% (30 year) and possibly lower. This is within a longer trend dynamic where they will likely move higher again thereafter. We would expect significantly higher yields in the next few years to materialise."

  Result: The down move in yields exceeded both the magnitude and timeframe (mid year) we expected but we do believe that October could have signaled the lows. **Grade: B+**

- "Gold finally looks to be forming a base for a move higher. However we need both more convincing price action and likely a struggling equity market to solidify this potential."

  Result: Gold did bounce as high as $1,392 (Quite a bit short of our potential $1,525 target) and is now virtually unchanged on the year. **Grade: B-**

- "In Local Markets the USDBRL chart is one of the more convincing pictures and suggests a much weaker BRL is in prospect in 2014."

  Result: Our target was 2.62. The high so far (hit in November) has been 2.6287. **Grade: A+**

- Overall: "We see a backdrop where the "repair process" of recent years continues at a slow pace but where the US continues to look like the "best house on a bad street" when it comes to the major developed nations. This should also benefit the USD and keep the relative picture for yields (monetary policy) in favour of the US."

  Result: This is pretty much how it has played out. In FX and LM the views came together very well. In fixed income the directional bias was correct but the extent of the move was underestimated. In housing things played out as expected. In Gold we got the correct directional bias but the move was not sustained and it looks like ending the year relatively unchanged. With regards to Consumer Confidence and the feedback to the Equity markets we underestimated the resilience of both in December last year but had changed our view by March.

- **Overall grade: A-**

(Note: All expectations in this document for 2014 were the views of the CitiFX Technicals team. They in no way constituted official Citigroup views.)

Outlook for 2015

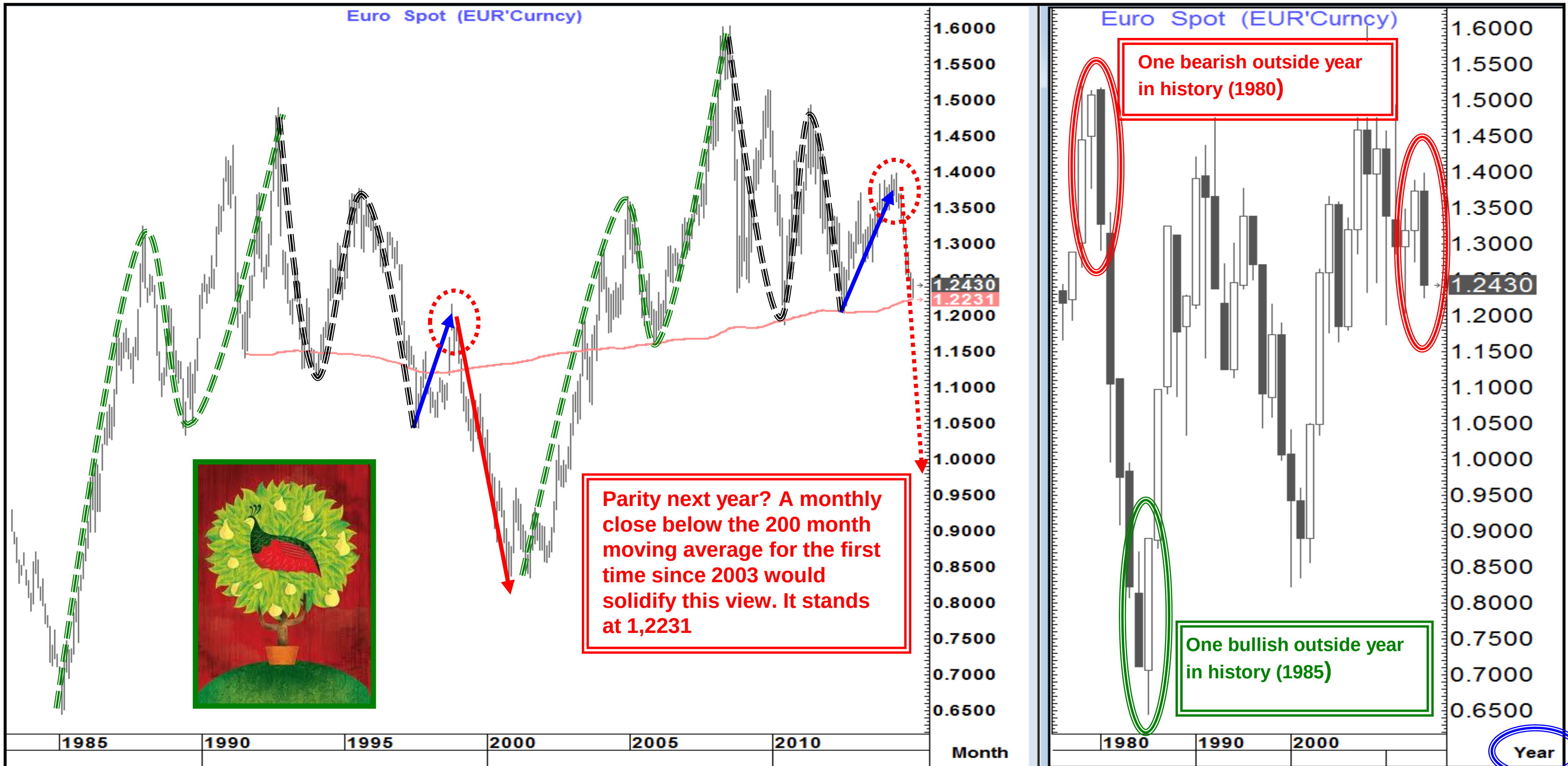
- In the rest of this note we give you our 12 Charts of Christmas. These are the 12 most important charts (in our view) that establish a "starting point" for our outlook on markets as we head into 2015.
- As always this will continue to be a work in progress over the course of 2015, but the pages ahead give you a sense of our strongest core views as we head into next year.

What do we believe for 2015?

- EURUSD bearish trend remains intact and we expect to see 1.10-1.15 levels in the first half of 2015, with parity or below possible over the year. Full QE from the ECB is likely early in the New Year
- European Bank Stocks Index may be the outperformer as the ECB further expands its balance sheet, with a move to at least 163 on the Index likely and an extension to the 240 area possible
- USDJPY trend looks bullish with levels above 130 likely in 2015
- Consumer Confidence (U.S.) looks set to continue to move higher as the economy improves. A robust U.S. economy will likely propel US Equity markets to new highs in 2015. Another double digit percentage return here would not be surprising in 2015.
- We expect to see NFP numbers head towards or above 400k, the Unemployment Rate decline towards 5%, and an elevated Core PCE potentially printing near 2.5%
- 2 year yields (U.S) will break the cycle of lower lows and lower highs and the Fed will start to normalise rates by June at the latest. The 2's versus 5's curve will bear flatten as the market anticipates this normalisation of monetary policy
- Crude oil (WTI) should regain some of its recent losses and could quite possibly head back towards $90 or above
- USDBRL looks likely to complete the double bottom around 2.62 and target as high as 3.70
- **Overall:** A more resilient economic/employment recovery in the US should be favourable for the USD and see US yields (in particular short end) head higher. Europe, along with the EURO, will continue to struggle. The backdrop for Equity markets overall should be positive, as a lot of liquidity remains in the system despite the withdrawal of accommodation by the Fed.

(Note All expectations in this document for 2015 are the views of the CitiFX Technicals team and in no way constitute official Citigroup views.)

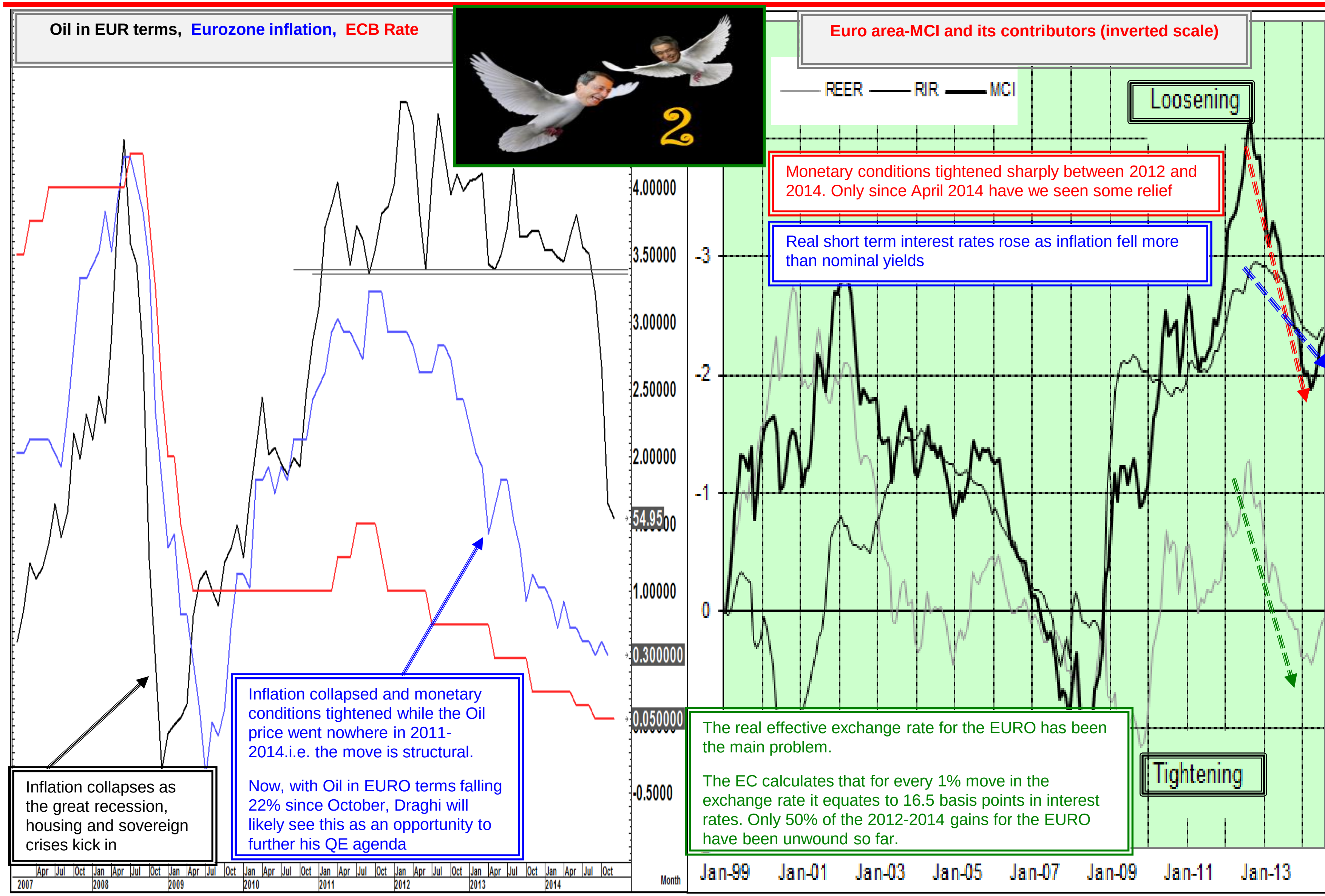
The 1st chart of Christmas truly says to me that in 2015 EURUSD heads below parity



Source: Aspen Graphics /Bloomberg December 10, 2014.

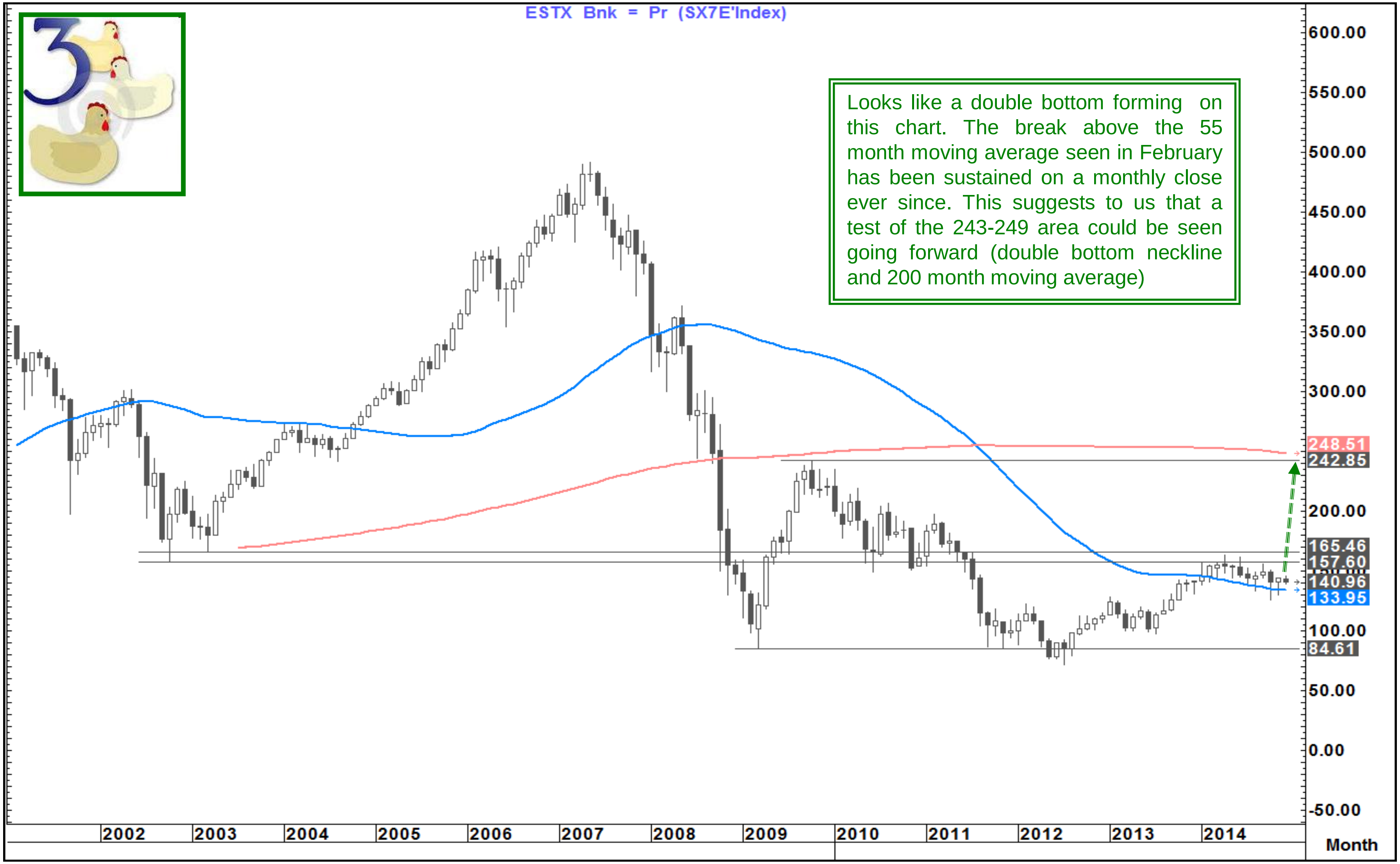
- For only the 2nd time in the history of floating exchange rates we are looking at the potential for a bearish outside **YEAR** in EURUSD.
- The only other time this happened was 1980, after which the USD rallied for another 4 years. There has also only once ever been a bullish outside year in EURUSD (1985), which was followed by 2 up years and a USD bear market that lasted 7 years (EUR as it's components).
- In 1981 (the year following the bearish outside year) EURUSD fell to a low **25%** below the 1980 close. In 1986 (the year following the bullish outside year) EURUSD rallied to a high **23%** above the 1985 close.
- **IF** we were to see a dynamic similar to the above next year it would suggest that EURUSD could trade below parity before the end of 2015
- In addition, a close above **84.75** on the USD-Index, if seen, would be a bullish outside year (Not shown).

The 2nd chart of Christmas truly says to me that very soon Draghi delivers full QE



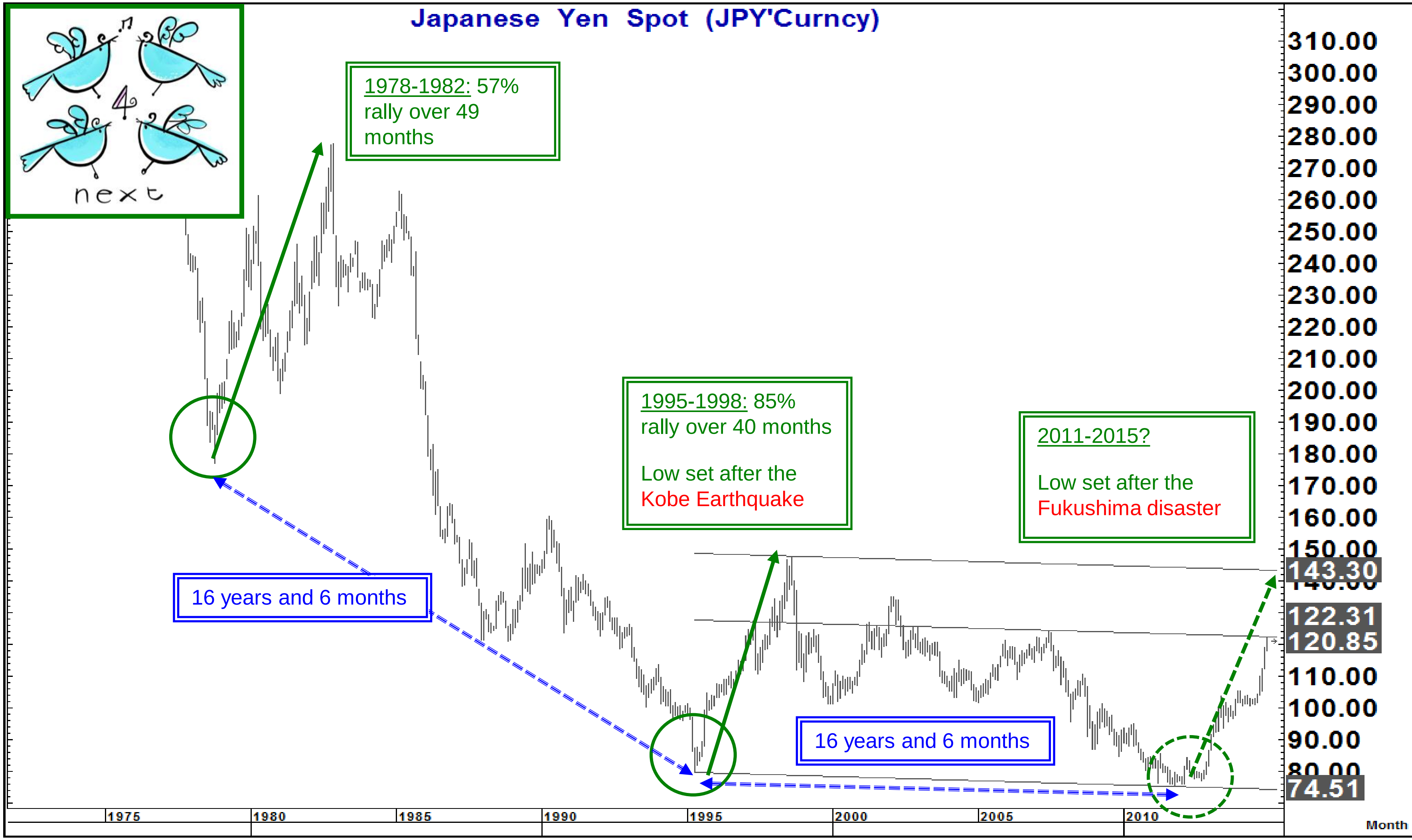
Source: Aspen Graphics /Bloomberg December 10, 2014.

The 3rd chart of Christmas truly says to me - European bank stocks to head higher on QE



Source: Aspen Graphics /Bloomberg December 10, 2014.

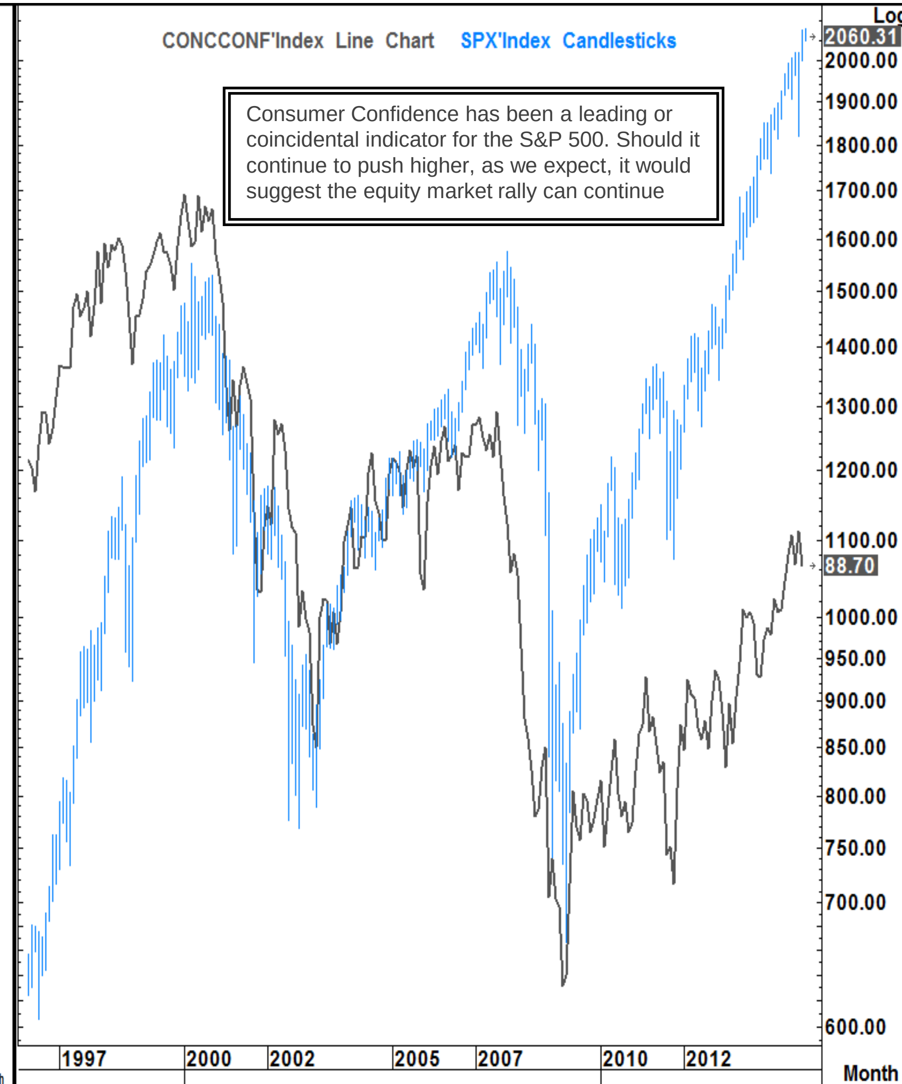
The 4th chart of Christmas truly says to me that “well north” of 130 on USDJPY we can see



Source: Aspen Graphics /Bloomberg December 10, 2014.

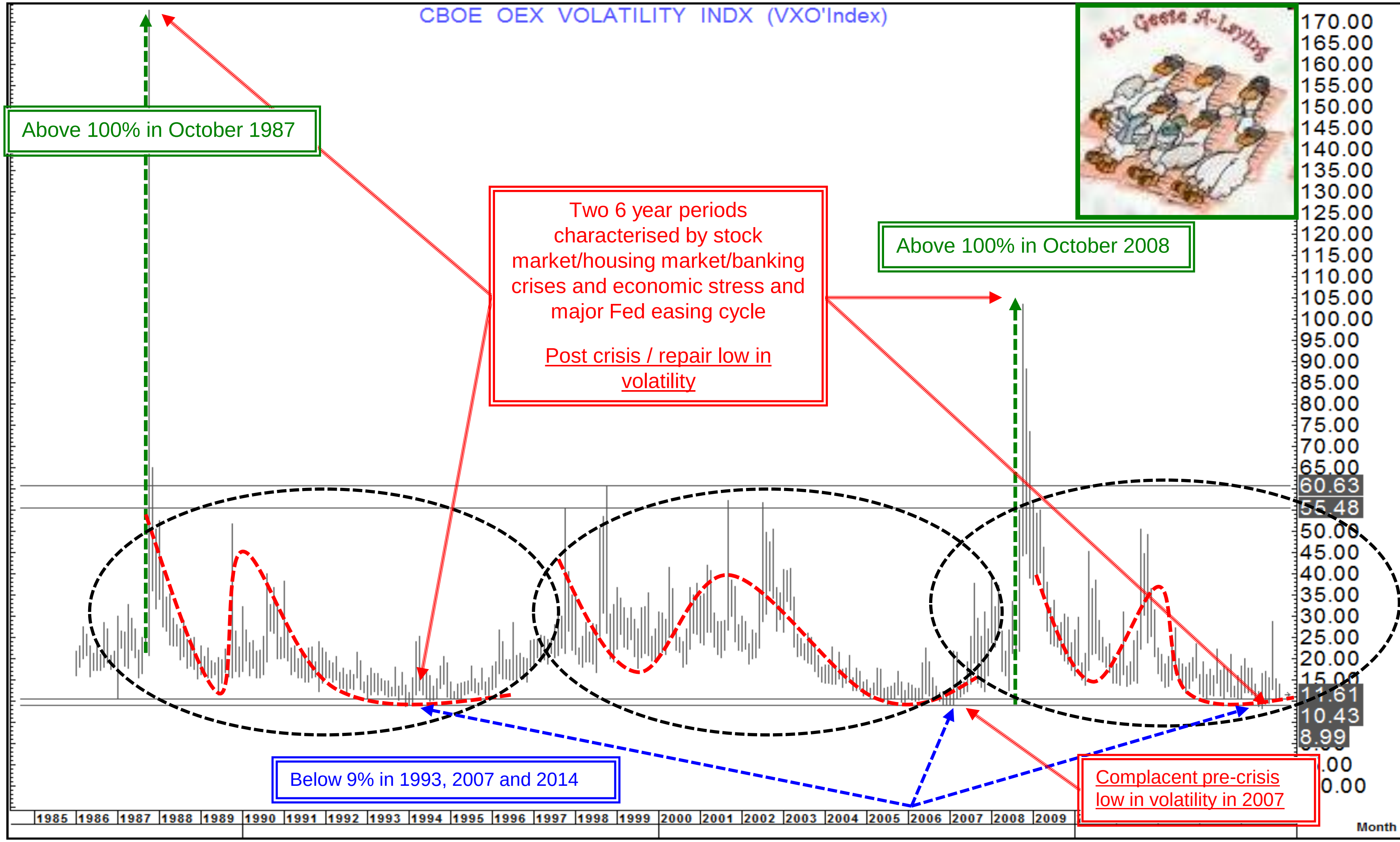
- A similar move in magnitude to the 1995-1998 period would suggest that **140** is “in the crosshairs”

The 5th chart of Christmas truly says to me that higher Consumer Confidence and S&P 500 we can see



Source: Aspen Graphics /Bloomberg December 10, 2014.

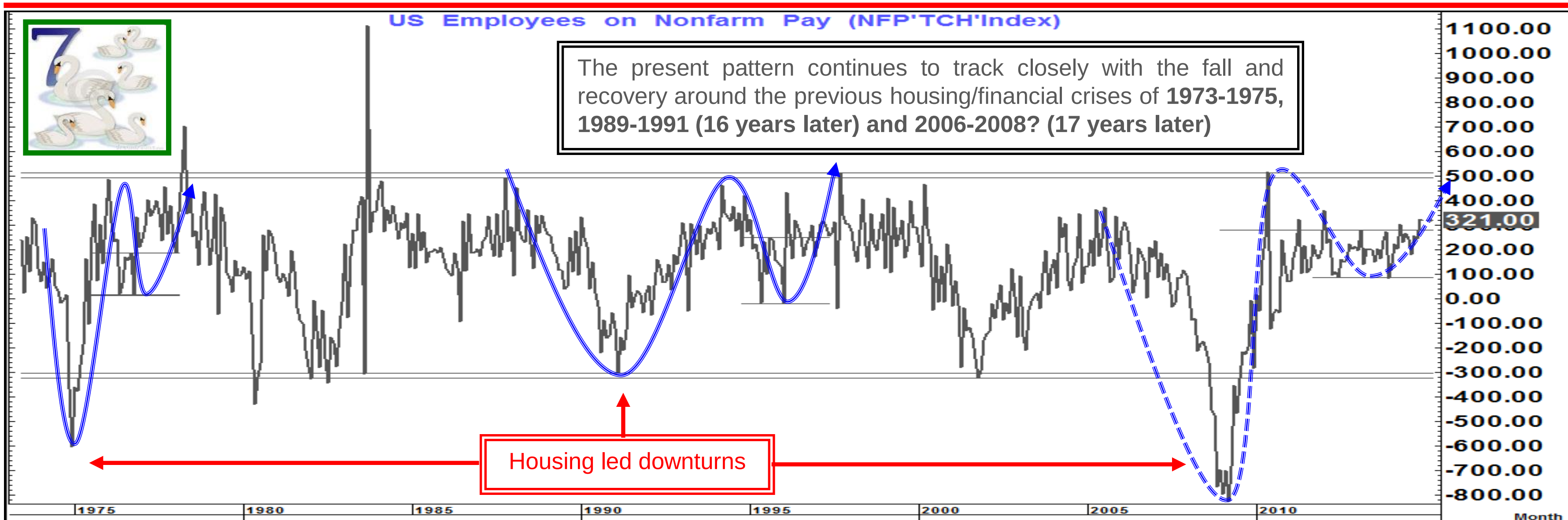
The 6th chart of Christmas truly says to me a positive U.S. Equity market we will see

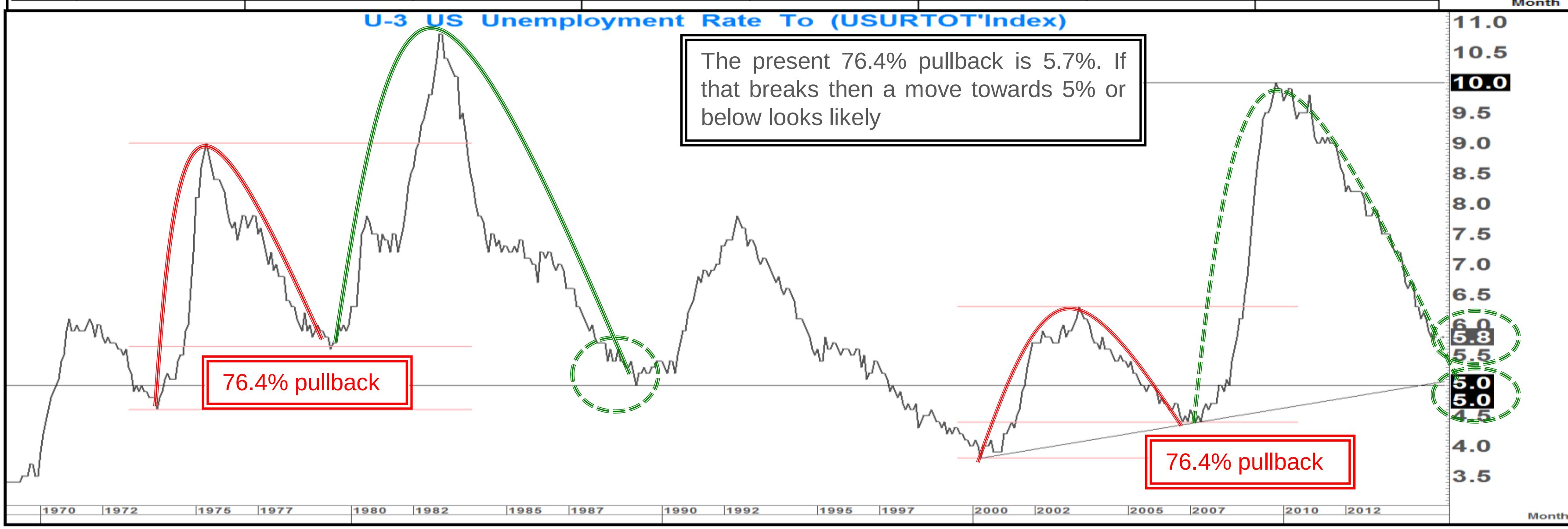


Source: Aspen Graphics /Bloomberg December 10, 2014.

- The present set-up in volatility is more like that seen in 1993/1994 than 2007. As a consequence, we suspect the trend low is in and a more normalised level of volatility can be expected in 2015 (more likely in the mid to high teens than single digits).

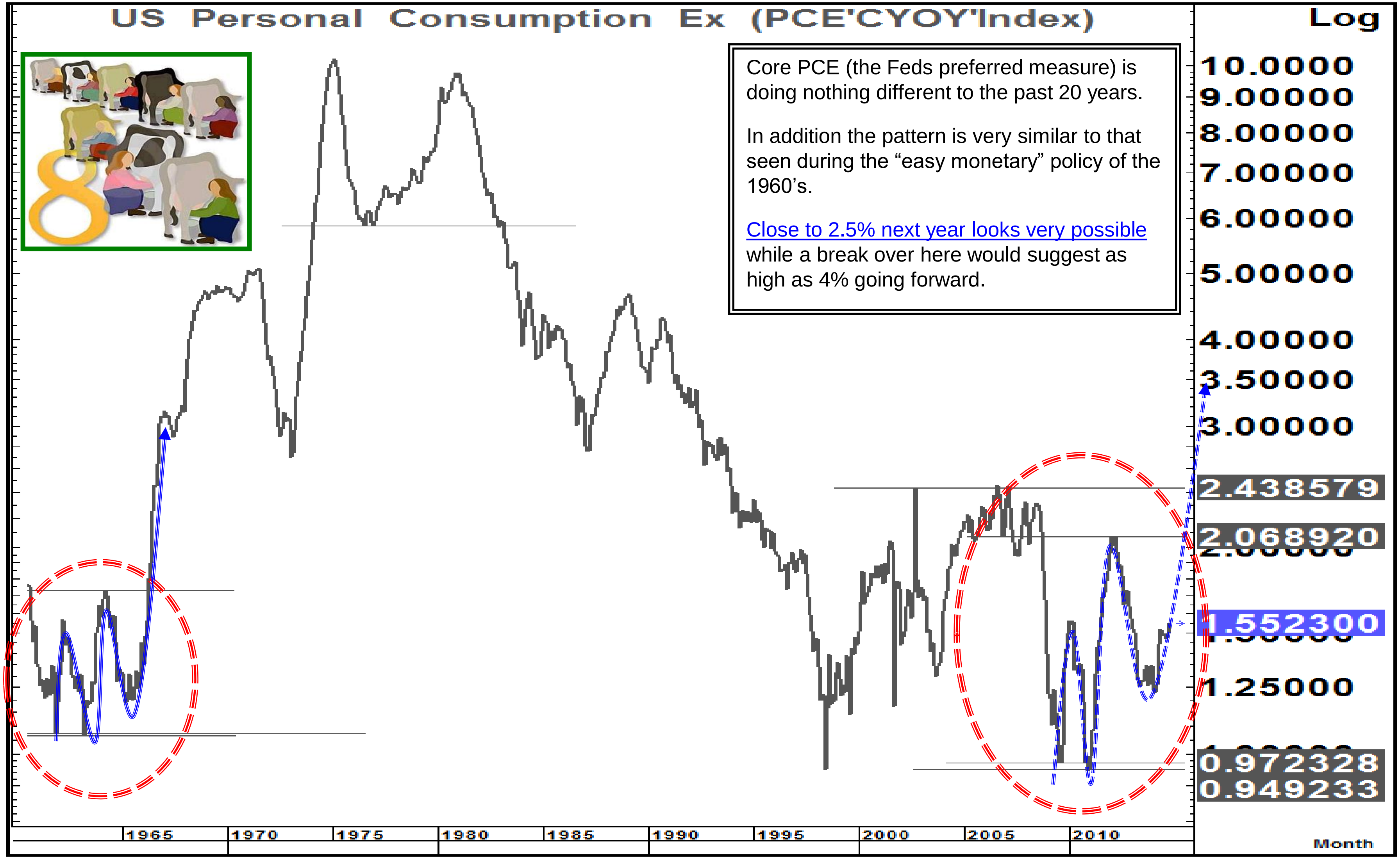
The 7th chart of Christmas truly says to me we see lower unemployment and a number over 400k on NFP





Source: Aspen Graphics /Bloomberg December 10, 2014.

The 8th chart of Christmas truly says to me that higher inflation we could see



Core PCE (the Feds preferred measure) is doing nothing different to the past 20 years.

In addition the pattern is very similar to that seen during the "easy monetary" policy of the 1960's.

Close to 2.5% next year looks very possible while a break over here would suggest as high as 4% going forward.

Source: Aspen Graphics /Bloomberg December 10, 2014.

The 9th chart of Christmas truly says to me a higher 2 year yield we could see

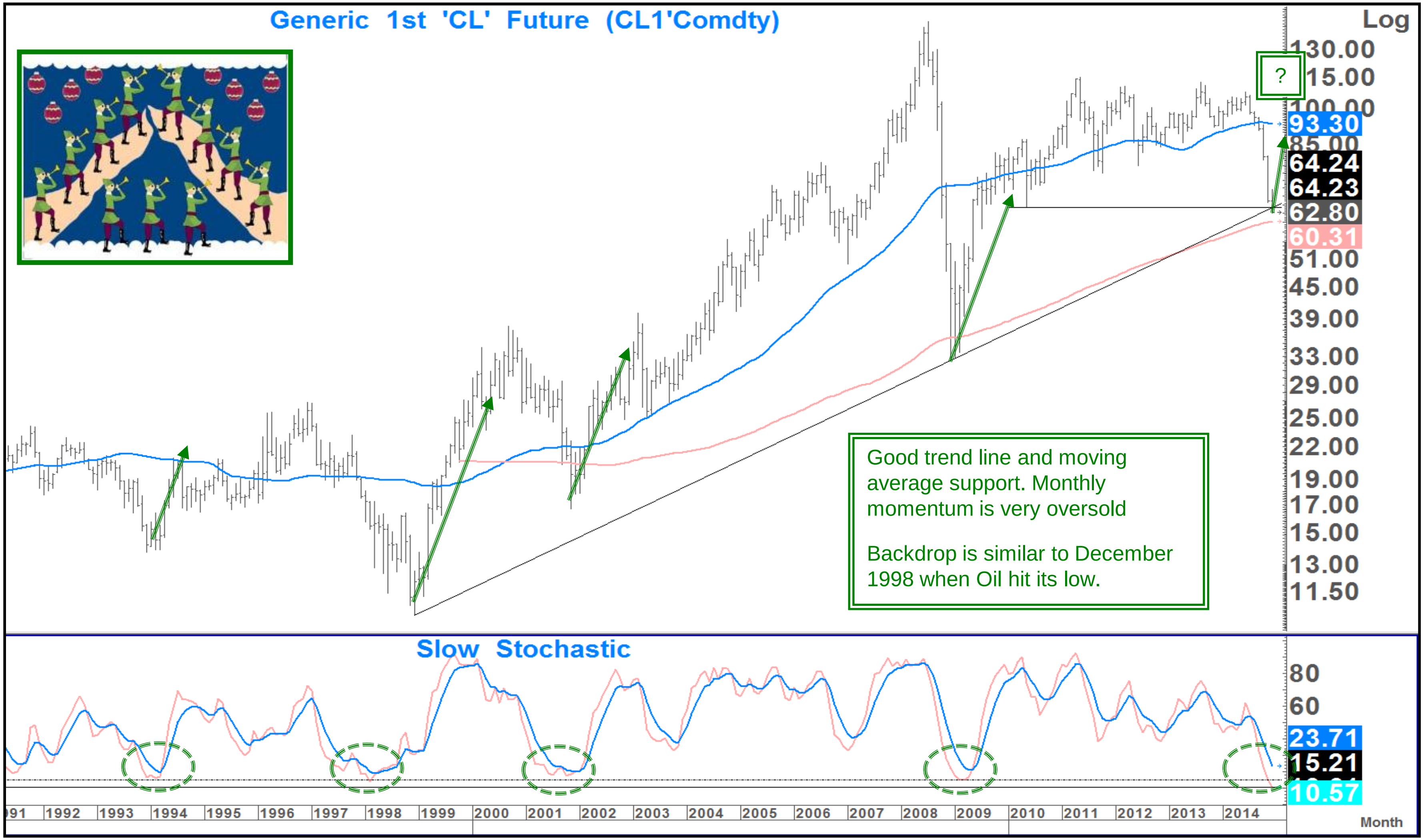
Source: Aspen Graphics /Bloomberg December 10, 2014.

- A monthly close this December above 56 bps would give an outside month (arguing for higher yields). The last time this happened was at the May 2013 lows. From the close that month we went 25 bps higher in less than 4 months.

The 10th chart of Christmas truly says to me a bear flattening in this curve …finally

Source: Aspen Graphics /Bloomberg December 10, 2014.

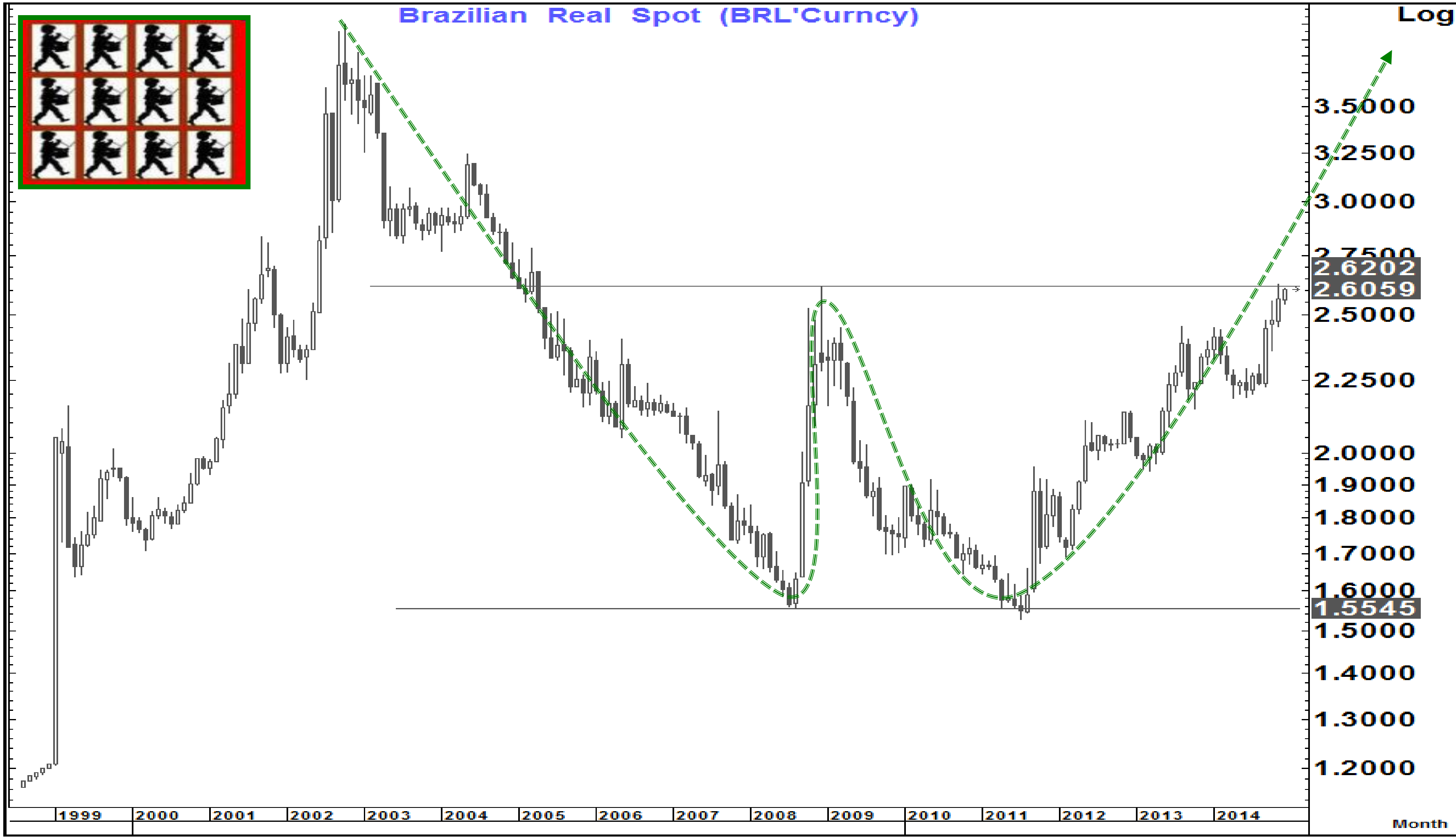
The 11th chart of Christmas truly says to me a renewed rally in Oil we shall see



Source: Aspen Graphics /Bloomberg December 10, 2014.

- A bounce back towards ~$90 or above looks likely over the next 12 months (WTI).

The 12th chart of Christmas truly says to me to keep an eye on Brazil's currency



Source: Aspen Graphics /Bloomberg December 10, 2014.

- A decisive break of 2.62 suggests much higher levels with a target as high as 3.70.

Summary of our strong conviction 2015 views

Instrument	View for 2014	Comment	Level today
EURUSD	▪ Move towards 1.10-1.15 in first half of 2015 with parity or below possibly later in the year.	Dynamics similar to those seen as we headed into 1999	1.2447
USDJPY	▪ Move into the 130's and possibly even close to 140.	Japanese domestic dynamics paired with Fed tightening should sustain this move	118.24
2 year yield (U.S.)	▪ A push above 89 basis points would suggest a move to the next resistance at 1.43%	Look for a test and likely break of 89 basis points to end the downtrend since 2007	56 basis points
2's versus 5's curve (U.S.)	▪ Bear flattening towards 50 basis points	As economy continues to build traction and the Fed raises short-term rates	100 basis points
S&P 500	▪ Another double digit percentage gain as it moves higher with Consumer Confidence	Recovering economy more positive for Equity markets than the Fed raising rates is negative	2,026
European Banks Index	▪ Strong rally initially towards 163 with 240+ possible longer term	QE by ECB should be very supportive of European bank stocks	138.34
Crude (WTI)	▪ Back to around $90 or above	Expect a recovery just as we saw after the major 1998 fall	$61.42
USDBRL	▪ Further gains expected. 3.70 target (ultimately) on a decisive break of 2.62	Long term double bottom potential remains valid	2.6166

Source: Aspen Graphics /Bloomberg December 11, 2014.

Contacts

Tom Fitzpatrick	Chief Technical Strategist	1-212-723-1344	thomas.fitzpatrick@citi.com
Shyam Devani	Senior Technical Strategist	65-6657-2964	shyam.devani@citi.com
Dan Tobon	Technical Strategist	44-207-986-3453	daniel.tobon@citi.com
Jay Bishen	Analyst	1-212-723-7057	jay.bishen@citi.com

Disclaimer

In any instance where distribution of this communication is subject to the rules of the US Commodity Futures Trading Commission ("CFTC"), this communication constitutes an invitation to consider entering into a derivatives transaction under U.S. CFTC Regulations §§ 1.71 and 23.605, where applicable, but is not a binding offer to buy/sell any financial instrument.

This communication is prepared by a member of the Sales and Trading Department of Citi which distributes this communication by or through its locally authorised affiliates (collectively, "Citi"). Sales and Trading Department personnel are not research analysts, and the information in this communication ("Communication") is not intended to constitute "research" as that term is defined by applicable regulations. Unless otherwise indicated, any reference to a research report or research recommendation is not intended to represent the whole report and is not in itself considered a recommendation or research report. All views, opinions and estimates expressed in this Communication (i) may change without notice and (ii) may differ from those views, opinions and estimates held or expressed by Citi or other Citi personnel.

This Communication is provided for information and discussion purposes only. Unless otherwise indicated, (i) it does not constitute an offer or recommendation to purchase or sell any financial instruments or other products , (ii) it does not constitute a solicitation if it is not subject to the rules of the CFTC (but see discussion above regarding communication subject to CFTC rules) and (iii) it is not intended as an official confirmation of any transaction. Unless otherwise expressly indicated, this Communication does not take into account the investment objectives or financial situation of any particular person. Recipients of this Communication should obtain advice based on their own individual circumstances from their own tax, financial, legal and other advisors before making an investment decision, and only make such decisions on the basis of the investor's own objectives, experience and resources. The information contained in this Communication is based on generally available information and, although obtained from sources believed by Citi to be reliable, its accuracy and completeness cannot be assured, and such information may be incomplete or condensed.

Citi often acts as an issuer of financial instruments and other products, acts as a market maker and trades as principal in many different financial instruments and other products, and can be expected to perform or seek to perform investment banking and other services for the issuer of such financial instruments or other products.

The author of this Communication may have discussed the information contained therein with others within or outside Citi and the author and/or such other Citi personnel may have already acted on the basis of this information (including by trading for Citi's proprietary accounts or communicating the information contained herein to other customers of Citi). Citi, Citi's personnel (including those with whom the author may have consulted in the preparation of this communication), and other customers of Citi may be long or short the financial instruments or other products referred to in this Communication, may have acquired such positions at prices and market conditions that are no longer available, and may have interests different from or adverse to your interests.

Investments in financial instruments or other products carry significant risk, including the possible loss of the principal amount invested. Financial instruments or other products denominated in a foreign currency are subject to exchange rate fluctuations, which may have an adverse effect on the price or value of an investment in such products. No liability is accepted by Citi for any loss (whether direct, indirect or consequential) that may arise from any use of the information contained in or derived from this Communication. Past performance is not a guarantee or indication of future results. Any prices provided in this Communication (other than those that are identified as being historical) are indicative only and do not represent firm quotes as to either price or size. You should contact your local representative directly if you are interested in buying or selling any financial instrument or other product or pursuing any trading strategy that may be mentioned in this Communication.

Although Citibank, N.A. (together with its subsidiaries and branches worldwide, "Citibank") is an affiliate of Citi, you should be aware that none of the financial instruments or other products mentioned in this Communication (unless expressly stated otherwise) are (i) insured by the Federal Deposit Insurance Corporation or any other governmental authority, or (ii) deposits or other obligations of, or guaranteed by, Citibank or any other insured depository institution.

IRS Circular 230 Disclosure: Citi and its employees are not in the business of providing, and do not provide, tax or legal advice to any taxpayer outside of Citi. Any statements in this Communication to tax matters were not intended or written to be used, and cannot be used or relied upon, by any taxpayer for the purpose of avoiding tax penalties. Any such taxpayer should seek advice based on the taxpayer's particular circumstances from an independent tax advisor.

Citi specifically prohibits the redistribution of this Communication in whole or in part without the written permission of Citi and Citi accepts no liability whatsoever for the actions of third parties in this respect.