

**SAXO
GROUP**

SAXO BANK PRESENTS

OUTRAGEOUS PREDICTIONS

For **2018**

Steen Jakobsen / Chief Economist / p5, p21
Peter Garrny / Head of Equity strategy / p9, p19
John J Hardy / Head of Forex strategy / p6, p11
Ole S Hansen / Head of Commodity strategy / p8
Kay Van-Petersen / Global Macro strategist
Jacob Pouncey / Cryptocurrency Analyst / p15
Christopher Dembik / Head of Macro Analysis / p13, p17

#SAXOSTRATS



OUTRAGEOUS PREDICTIONS

For **2018**

- **Fed loses independence as US Treasury takes charge**
Treasury enacts 2.5% yield cap after massive spike
- **Bank of Japan loses control of its monetary policy**
USDJPY rises to 150 and then collapses to 100
- **China issues CNY-denominated oil futures contract**
Petro-renminbi surges, USDCNY below 6.0
- **Volatility spikes on sudden S&P 500 'flash crash'**
S&P 500 drops 25% in spectacular plunge
- **US voters push left in 2018 mid-terms, bonds spike**
US 30-year Treasury yields rip beyond 5%
- **'Austro-Hungarians' launch hostile EU takeover**
EURUSD to 1.00 after hitting new highs
- **Investors flee Bitcoin as governments strike back**
Bitcoin @ \$1,000
- **South Africa resurgent after 'African Spring'**
ZAR gains 30% versus EM currencies
- **Tencent topples Apple as market cap king**
Tencent shares gain 100%
- **Women take the reins of corporate power**
Female CEOs at more than 60 Fortune 500 companies



SAXO BANK'S 2018 OUTRAGEOUS PREDICTIONS

by #**SAXO**STRATS

We've delved deep again this year in penning our annual list of 10 Outrageous Predictions. As usual, we roam the world and ride roughshod over consensus in sniffing out these supposedly highly unlikely events with underappreciated potential – events that could have tremendous implications if they come to pass. Enjoy!

2017 was supposed to be the year of volatility. We entered the year with existential concerns in Europe ahead of key national elections, US policy concerns due to bull-in-the-china-shop President-elect Donald Trump, and Chinese policy concerns as markets eyed October's 19th Party Congress. All in all, it seemed as if this would be the year we would see more a more rambunctious monetary policy impulse and more dramatic gyrations in global markets.

Instead, the EU elections went off smoothly on balance while the European Central Bank's supply of quantitative easing morphine kept Continental equities on a pleasant high despite a sharply stronger euro.

In the US, Trump floundered from one scandal and gaffe to the next, entirely failing to pull any policy levers that impacted markets even as he took personal responsibility for a stellar year in equity markets with record low volatility.

In Asia, China's desire to keep everything orderly until at least the other side of the Party Congress kept fears of a renminbi devaluation on ice and the economy in reasonable shape even as the country's dangerous credit bubble inflated further.





In short, with few exceptions, global risk assets enjoyed a very good year with very low volatility – the kind of year very few predicted and thus an outrageous one indeed, especially for bears and gold bugs. Who would have thought that, 12 months after the 2016 Election Day earthquake in the US, a classic fear indicator like gold would be near-precisely unchanged!

Our suspicion is that the complacency and low volatility in 2017 will not repeat and may indeed have stored energy for a spectacular and outrageous 2018. Thus, a number of our predictions point squarely at the risk that this accumulation of excess complacency may have blown a pent-up bubble of volatility.

But do keep in mind, as always, that these are not forecasts. Rather, they are a list of supposed “1% likelihood” events that should really be considered as 10% likely... or higher.

Besides our prediction of an ugly end to the complacency bubble, we place our European focus on the increasingly stark political faultline between “Austro-Hungarian Europe” and its feasible allies, and the traditional EU core.

In China, we look at the potential for enormous gains in consumption-linked equities as China transitions from an investment to a consumption-focused growth model. We wax outrageously bullish on sub-Saharan Africa and equally bearish on central banks, who risk having their independence taken away next year.

It's safe to say that if any of our predictions see the light of day in 2018, the world will feel like a new place this time next year.



FED LOSES INDEPENDENCE AS US TREASURY TAKES CHARGE

Steen Jakobsen / Chief Economist



The independence of the US Federal Reserve has historically fluctuated according to the needs and policies of the federal government. In 2018, it will lose significant ground as Washington moves to cap government yields in the face of a bond market meltdown.

The independence of the US Federal Reserve Bank was restored by the 1951 Accord after it lost much of its independence in the post-World War II period due to the government's need to cap yields. This yield-capping came as wartime price controls were lifted and in light of the government having taken on enormous wartime debts.

Indeed, the 104-year history of the Fed shows a number of smaller and larger swings in its power and ability to act independently. In 2018, the pendulum swings away from the Fed's favour as the Treasury takes on emergency powers and forces the central bank to cap US government yields to prevent a bond market meltdown.

Both the Republican and Democratic parties will increasingly vie for their share of the populist vote heading into 2018's mid-term elections, and budget discipline is entirely absent with GOP tax cuts bringing a massive revenue shortfall that will only be made worse as the US heads into recession.

The double whammy of a weak economy and higher interest rates/inflation will leave the Fed with no answers on monetary policy.

The hapless Fed will be scapegoated by politicians for the economy's weak performance, a bond market in vicious turmoil, and the aggravation of already worsening inequality brought on by years of post-global financial crisis quantitative easing.

In order to maintain federal spending and nominal growth, as well as to stabilise the bond market and save face into the 2018 mid-terms, ***the US Treasury seizes the reins as it did after World War II, enacting the same 2.5% yield cap on long bonds after a massive spike in yields.***



BANK OF JAPAN FORCED TO ABANDON YIELD CURVE CONTROL

John J Hardy / Head of FX strategy



The Bank of Japan's policy of yield curve control depends on soft global interest rates and low yields, and in 2018 this centre will simply not hold. As inflation rises, yields too will spike, and the result will be a fantastical plunge in the yen. Ultimately, the central bank will need to resort to QE-style measures, but not before USDJPY hits 150.

The Bank of Japan's yield curve control policy was always a luxury predicated on interest rates remaining orderly elsewhere in the world. After all, a continued rise in global yields would eventually mean that maintaining the 10-year JGB "peg" would transfer all of the pressure onto the yen.

The Bank of Japan was already forced to defend the peg twice in 2017. In market history, pegs are like rules – they are made to be broken. The world enters 2018 completely complacent on inflation risks, and these rise as spare capacity in key skilled wage industries disappears and China preserves yuan strength while maintaining high nominal growth rates in an effort to devalue its credit excess via inflation.

With inflation rising and global bond yields (led by US Treasuries) surging, the BoJ nevertheless digs in its heels on the 10-year yield peg and even tries to make a show of moving the peg slightly to accommodate market pressures. The JPY is crushed all the way to 150 versus USD in an aggravated spike to absorb the pressure of higher yields.

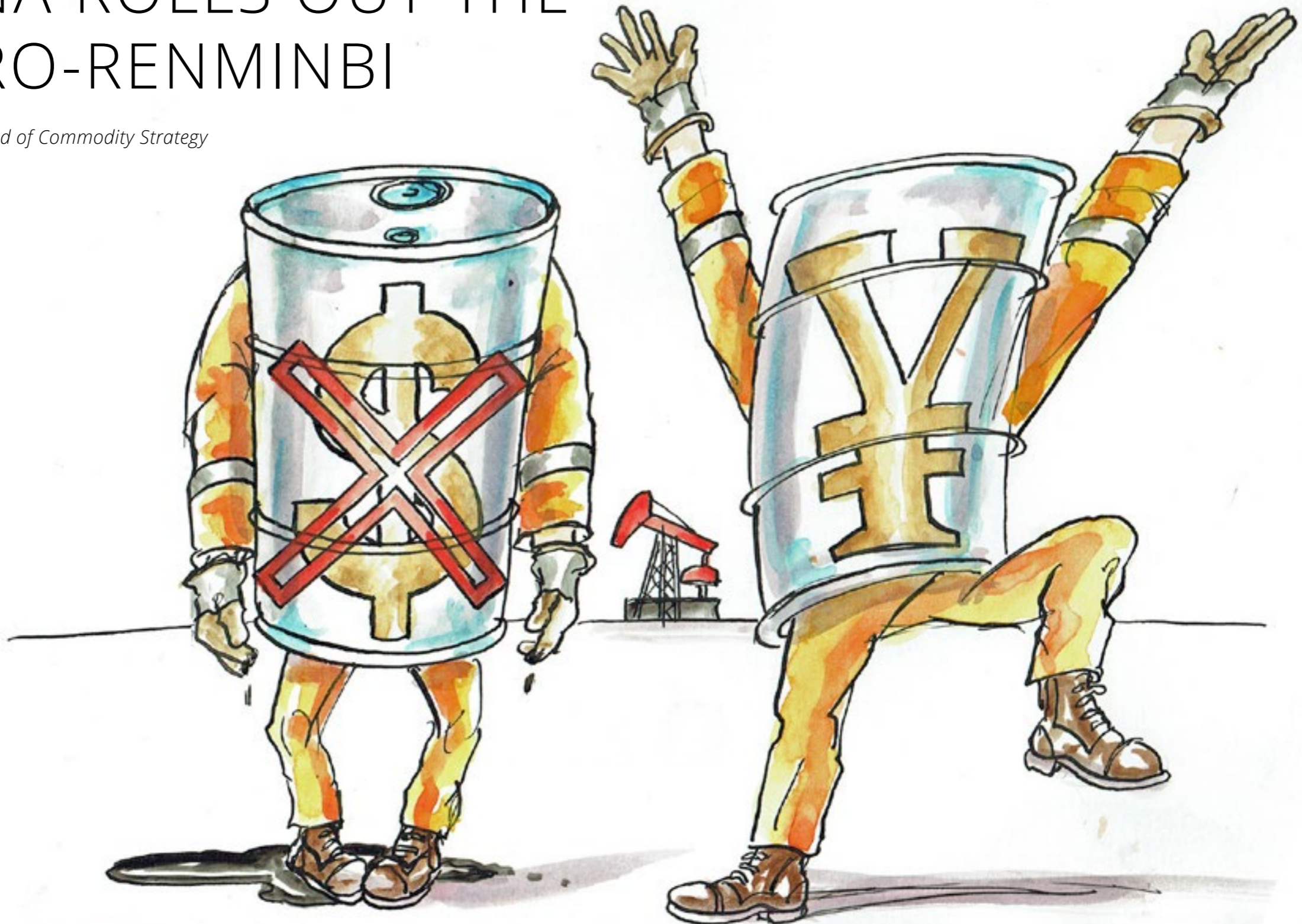
Then, amidst criticism from global peers on the BoJ's policy and the competitive advantages that the weak yen provides Japan – as well as ugly popular resentment due to an imports-driven spike in the cost of living – the BoJ is forced to capitulate and revert to simple, "mopping up"-style quantitative easing operations to prevent JGB yields from surging out of control.

USDJPY hits 150 before the BoJ capitulates, after which it rapidly devalues to 100.



CHINA ROLLS OUT THE PETRO-RENMINBI

Ole Hansen / Head of Commodity Strategy





CHINA ROLLS OUT THE PETRO-RENMINBI

Ole Hansen / Head of Commodity Strategy



China is by far the world's largest oil importer, and many producer nations are already more than happy to transact in yuan terms. With the US' global power and reach waning, and given the success of CNY-based commodity futures in general, the Shanghai International Energy Exchange's decision to launch a yuan-based crude oil future is a runaway success.

2018 marks the year in which the Shanghai International Energy Exchange finally launches an oil contract denominated in Chinese yuan, a move with tremendous geopolitical and financial consequences.

The global futures market for oil trading has for years been governed by the dollar-denominated benchmarks of West Texas Intermediate and Brent crude. Combined, these represent a daily turnover of more than two billion barrels – some 20 times the total daily world oil demand.

In recent years, the US WTI crude oil contract has been increasingly sidelined by the seaborne Brent crude oil contract as the global benchmark against which many other oil qualities are priced. China, meanwhile, has already become far and away the world's largest crude oil importer and many key exporters – led by Iran and Russia – are more than happy to transact in yuan terms.

This is both because China has effectively allayed fears that it will devalue its currency and to thumb their noses at the US due to fraught relations with the declining superpower.

Reserve managers in these countries diversify currency holdings into yuan at the cost of USD in particular, but also the euro as China maintains a stable, high value for its currency. As with other CNY-based commodity futures launched over the past few years (especially in metals), the oil contract becomes a raging success.

The introduction of the petro-yuan sees CNY appreciate more than 10% versus the dollar, taking the USDCNY rate below 6.0 for the first time ever.



VOLATILITY SPIKES AFTER FLASH CRASH IN STOCK MARKETS

Peter Garnry / Head of Equity Strategy



World markets are increasingly full of signs and wonders, and the collapse of volatility seen across asset classes in 2017 was no exception. The historic lows in the VIX and MOVE indices are matched by record highs in stocks and real estate, and the result is a powder keg that is set to blow sky-high as the S&P 500 loses 25% of its value in a rapid, 1987-esque flash crash.

Investors have experienced many extraordinary events over the past 10 years and 2017 was no exception. In fact, it was truly extraordinary year as volatility across asset classes collapsed and the MOVE index of bond market volatility and VIX index of equity volatility posted all-time-lows during the year.

At the same time, credit and government bonds are historically very expensive. Equities and real estate are also flirting with record levels... good times, right? Not really, because the drivers of bubbly asset prices – quantitative easing, interest rate targeting, and low/negative rates – are aggravating imbalances and weakening the financial system. It's no secret that 2018 will see the Federal Reserve reduce its balance sheet at an accelerating pace while the European Central bank halves its QE purchases from January 1.

Another layer of danger can be found in the fact that much of the upside in assets has been driven by blind and massive inflows into passive investment vehicles, smart beta funds, "risk parity" asset allocation funds, and highly risky short volatility strategies.

It's estimated that around \$800 billion sits in risk parity strategies across funds and discretionary accounts. With low returns offered in bonds and given the flattening yield curve, risk parity funds will have to increase leverage to meet volatility targets, causing underlying risk to go up.

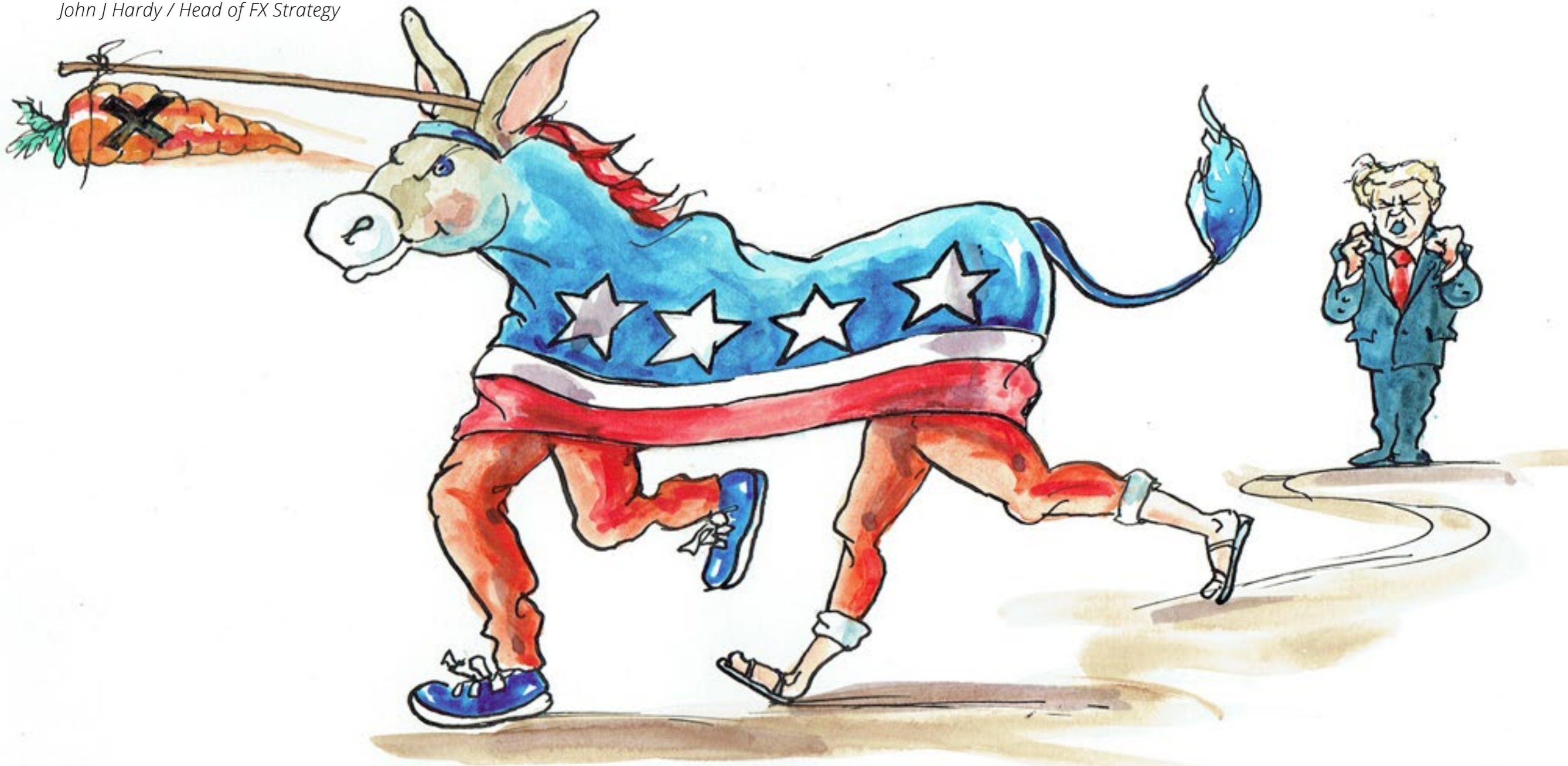
In short, it's a powder keg – any policy or shock could trigger a flash crash in multiple markets with risk parity funds acting as an amplifier as investors pile into cash.

For these reasons, **the S&P 500 suffers a flash crash of 25% (peak-to-trough) in a spectacular, one-off move reminiscent of 1987. A whole swathe of short volatility funds are completely wiped out and a formerly unknown long volatility trader realises a 1000% gain and instantly becomes a legend.**



US VOTERS GO HARD LEFT IN 2018 ELECTION

John J Hardy / Head of FX Strategy





US VOTERS GO HARD LEFT IN 2018 ELECTION

John J Hardy / Head of FX Strategy



Changing demographics in the US which already have the under-35 millennials in place as a larger cohort than the post-war baby boomers will have a dramatic impact on politics in 2018. One outcome will be a spiralling public deficit.

Much has been made of the Trump brand of populism. But let's not forget the Bernie Sanders revolution that was nearly as popular and was only short-circuited by the Clinton political machine in the 2016 primaries.

In 2018, populism on both sides won't be denied and the US mid-term elections see a hard turn left as a strong majority go all-in for European-inspired democratic socialism, the largest political earthquake in a generation. As Trump's former strategist Steve Bannon stated in a 60 Minutes interview on the political lay of the land: "the only question before us is whether it's going to be a left-wing populism or a right-wing populism... and that is the question that will be answered in 2020."

We agree, except that it is already crunch time in 2018 and the Democrats easily take back both houses of Congress. The future of any country is in its younger generation, and the under-35 millennials are now America's largest generation, larger even than the vaunted baby boomers. They also wear a very different set of political stripes as they showed in a groundswell of support for social democrat Bernie Sanders in 2016.

The general revulsion of younger voters for Trump's persona, the widening inequality gap aggravated even further by the Republicans' cynical tax reform, and a new breed of Democratic candidates who are unafraid to tap into Sanders-style populism from the left see millennials turning out in droves at the polls in November.

The Democrats pull the debate away from tax reform to spending stimulus for the masses. **True populism means breaking out the chequebook for the 90%, and that means fiscal stimulus, deficits be damned. US 30-year Treasury yields rip beyond 5%**



'AUSTRO-HUNGARIAN EMPIRE' THREATENS EU TAKEOVER

Christopher Dembik / Head of Macro Analysis





'AUSTRO-HUNGARIAN EMPIRE' THREATENS EU TAKEOVER

Christopher Dembik / Head of Macro Analysis



The divide between old core EU members and the more sceptical and newer members of the bloc will widen to an impassable chasm in 2018 and will shift the centre of gravity from the Franco-German axis to Visegrad-and-friends. The consequences for the euro will be severe.

Diplomatic tensions between Western and Eastern Europe spiked in 2017 on the issues of expatriate workers, migrant quotas, and democratic values. In 2018, the tensions go from bad to worse.

The ambitious French leader, Emmanuel Macron, who is already planning to run for president of Europe, convinces Germany and its weakened chancellor Angela Merkel, as well as the three Benelux countries, to integrate further and create a joint treasury and a common defence budget. Opposed to further integration, CEE leaders fear that such a move would significantly reduce their political influence within the European Union.

Echoing the old outlines of the Austro-Hungarian Empire, the new Austrian chancellor – who has successfully formed an ÖVP–FPÖ coalition government – decides to join the Visegrad Group, which gathers the four least Europhile members of the EU (besides the exiting UK). He moves closer to Hungary's populist premier Viktor Orban on economic and migration issues which results in a Franco-German diplomatic boycott against Austria. Tensions reach a climax when the European Commission, urged on by France, Belgium and Germany, launches an Article 7 procedure against Poland for its disrespect for the rule of law.

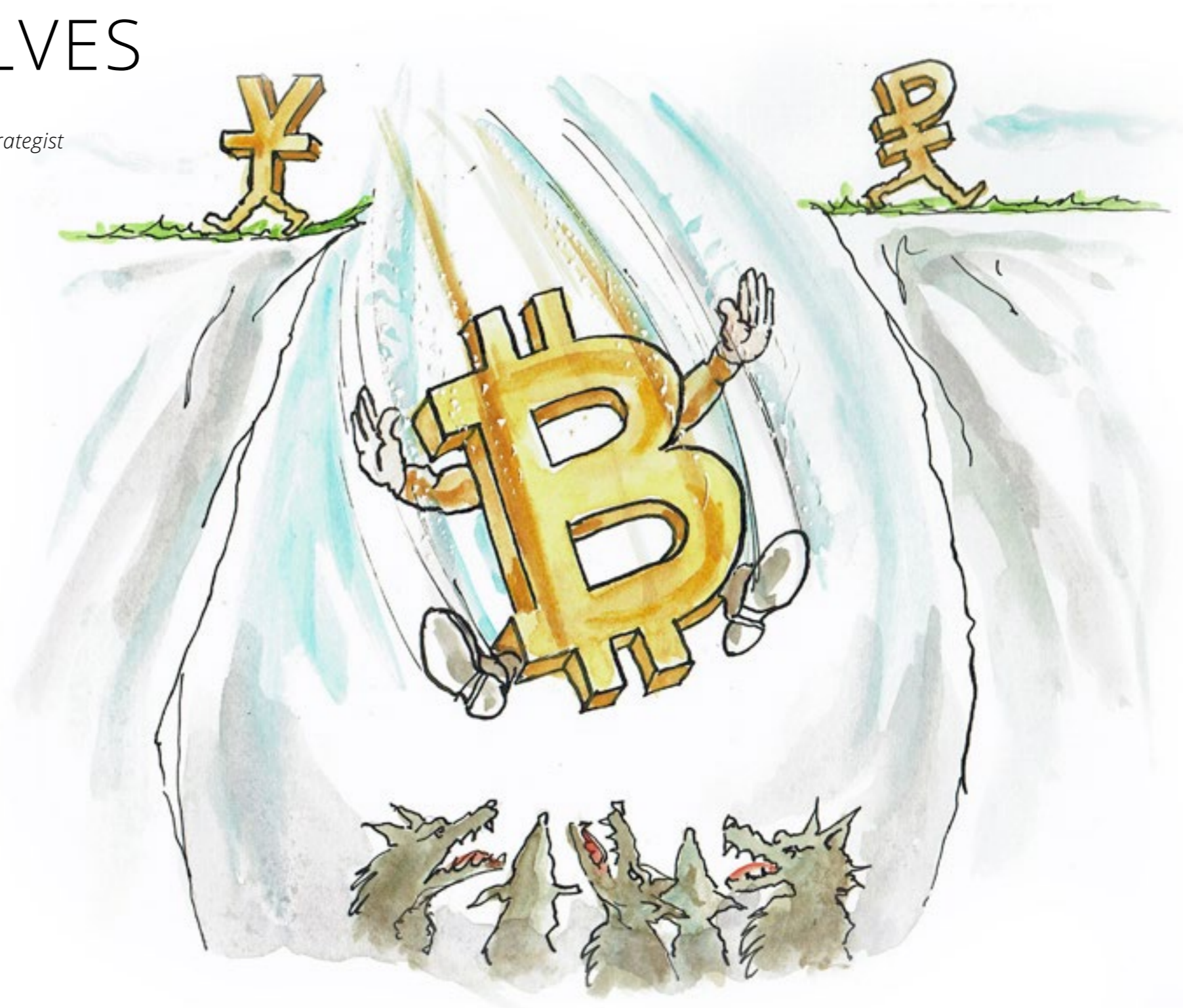
Looking for further weight to counter the Franco-German led “core EU”, Austria and the Visegrad 4 lobby to take the union in a pro-stimulus and anti-immigration direction. They successfully manage to gather a group of 13 EU countries, including Italy (once again led by Silvio Berlusconi) and Slovenia, to form a blocking minority at the European Council.

For the first time since 1951, Europe's political centre of gravity shifts from the Franco-German couple to CEE. The EU's institutional blockage does not take long to worry financial markets. **After spiking to new highs versus the G10 and many EM currencies by late in 2018, the euro rapidly weakens towards parity with USD.**



BITCOIN IS THROWN TO THE WOLVES

*Kay Van-Petersen / Global Macro & Crypto Strategist
Jacob Pouncey / Cryptocurrency Analyst*





BITCOIN IS THROWN TO THE WOLVES

*Kay Van-Petersen / Global Macro & Crypto Strategist
Jacob Pouncey / Cryptocurrency Analyst*



The rise of Bitcoin and other cryptocurrencies has been one of the most spectacular phenomena of financial markets in recent years. Bitcoin will continue to rise – and rise high – during most of 2018 but Russia and China will together engineer a crash.

Bitcoin peaks in 2018 with Bitcoin above \$60,000 and a market capitalisation of over \$1 trillion as the advent of the Bitcoin futures contract in December 2017 leads to a groundswell of involvement by investors and funds that are more comfortable trading futures than tying up funds on cryptocurrency exchanges.

Before long, however, the Bitcoin phenomenon finds the rug torn out from under it as Russia and China move deftly to sideline and even prohibit non-sanctioned cryptocurrencies domestically. Russia officially enters the cryptocurrency mining space to influence protocol developments and shift the focus away from Bitcoin in an effort to keep more Russian capital onshore. China makes a similar move, cracking down on cryptocurrencies by banning the mining of the most popular ones within China, citing energy waste and environmental concerns, but likewise fearing the risk of Bitcoin as a vehicle for capital flight.

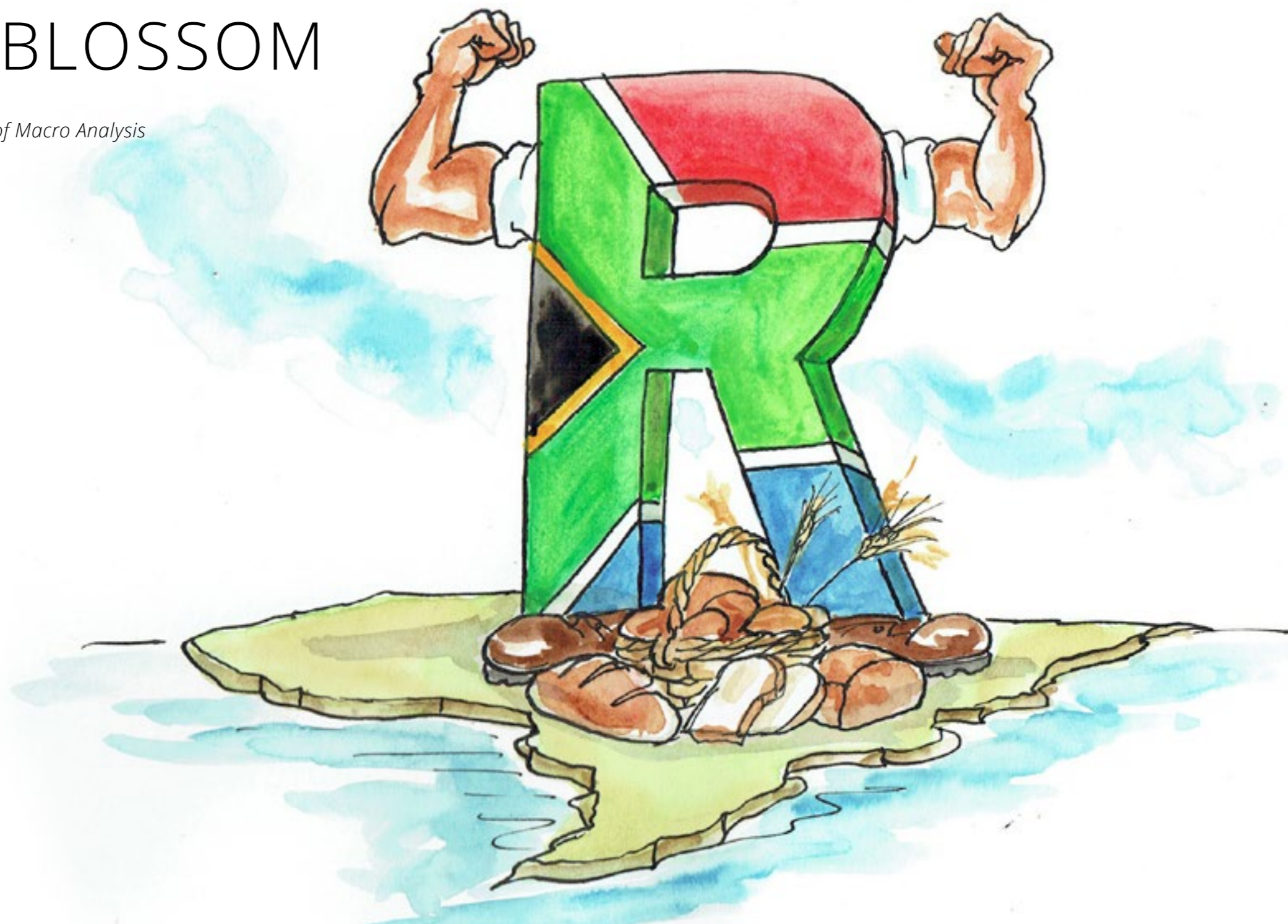
Instead, China launches an officially backed cryptocurrency that entails less energy-intensive mining. The smoother functioning of the state-run protocols for actual payments and price stability, as well as the heavy hand of state intervention, drives a decreasing interest in all cryptocurrencies and completely sidelines the Bitcoin and crypto phenomenon from a price speculation angle even as the technological promise of the blockchain gallops on.

After its spectacular peak in 2018, Bitcoin crashes and limps into 2019 close to its fundamental “production cost” of \$1,000.



SOUTHERN AFRICAN SPRING SEES SOUTH AFRICA BLOSSOM

Christopher Dembik / Head of Macro Analysis





SOUTHERN AFRICAN SPRING SEES SOUTH AFRICA BLOSSOM

Christopher Dembik / Head of Macro Analysis



The Arab Spring, which was once a harbinger of hope for many millions of people across North Africa, has now faded to dust. But Africa always has the potential to surprise us and 2018 will see South Africa lead an unexpected renaissance that will see it and its neighbours blossom politically and economically.

The democratic uprisings of the Arab Spring of 2010-2011 were supposed to bring peace and prosperity to North Africa and the Middle East but some six years after the old leaders were thrown out, Egypt is mired in turmoil and inflation and Tunisia faces mass unemployment

In 2018, after a surprising turn of events, a wave of democratic transition spreads across sub-Saharan Africa. The forced resignation of Zimbabwe's long-term president Robert Mugabe at the end of 2017 triggers a wave of political change in other African countries upset with their leaders' out-of-touch and ineffective leadership. South Africa's Jacob Zuma is forced out of power and Congo's Joseph Kabila faces unprecedented demonstrations pushing him to flee the country. New leaders take power and announce that free and fair elections monitored by international organisations will take place in the course of the year. In the meantime, the international business community, faced with a dearth of growth prospects in advanced and emerging economies, pours money into investments in the rapidly liberalising region.

Good governance and social progress are the watchwords as Africa begins to realise its tremendous potential.

The first positive economic consequences do not take long to fully materialise for these three countries: Zimbabwe rapidly emerges from hyperinflation and once again becomes Africa's agricultural breadbasket. FDI inward flows in the Democratic Republic of the Congo reach a record high of \$10 billion in 2018, driven particularly by the country's cobalt reserves.

South Africa, however, is the main winner as **the ZAR becomes the EM darling and returns 30% against the G3 currencies. It brings the world's strongest rates of growth in South Africa and the satellite frontier economies of the region.**



TENCENT OUTSTRIPS APPLE, BECOMES WORLD'S LARGEST COMPANY

Peter Garnry / Head of Equity Strategy





TENCENT OUTSTRIPS APPLE, BECOMES WORLD'S LARGEST COMPANY

Peter Garnry / Head of Equity Strategy



China is opening up its capital markets, and the country's enormous size and surging living standards are attracting investors from across the globe. Given this, it's no surprise that tech-sector leader Tencent is bumping up against some of the world's largest companies by market capitalisation. In 2018, though, all of this jostling for position will become a thing of the past as Tencent leaves its US rivals in the dust.

China, still the world's most populous country and one with a rapidly rising standard of living, is opening up its capital markets and its reform programmes are driving a fresh rise in investor sentiment after missteps in 2015.

The focus is particularly intense when it comes to Chinese technology stocks with market leader Tencent's shares rocketing 120% higher in 2017. The exorbitant rally was fuelled by explosive topline revenue growth of over 60% (year-on-year) in Q3 and a rise of some 50% in operating income.

In fact, Tencent is the only \$100 billion-plus market capitalisation giant in the world that is generating this kind of growth. It's not surprising, however, given that the firm is a world leader in the red-hot eSports market (with 60 million viewers of its League of Legends games) and continues to surprise the market in successfully monetising Facebook-equivalent WeChat's billion-plus active user base.

In late 2017, Tencent moved into the global top five in market cap terms, nearing \$500 billion and even eclipsing Facebook at one point. In 2018, though, Tencent leaves the other giants in the dust – even if a wildly successful iPhone X takes Apple's market cap to \$1 trillion.

On top of its own successful business model, Tencent's success is driven by China's transition to a more consumption-led economy. **Tencent shares advance another 100% despite the company's already enormous size and in 2018 the firm steals the world market cap crown from Apple at well above \$1 trillion.**



IT'S THEIR TIME – WOMEN SMASH THE GLASS CEILING

Steen Jakobsen / Chief Economist





IT'S THEIR TIME – WOMEN SMASH THE GLASS CEILING

Steen Jakobsen / Chief Economist



Women have long been underrepresented in the corridors of power but this will change and change fast in 2018 as more and more females get to lead the world's biggest companies. The revolution will be sparked not by a desire to right an historical wrong but rather, by an incontestable economic imperative.

In 2018, the trend towards increasing female representation in the boardroom level goes super-exponential, with twice as many women rising to the level of CEO at Fortune 500 companies. Over the last generation, women have started achieving higher education levels than men, with US universities now graduating some 50% more women than men at the bachelor's degree level. Women also now comprise nearly half of all business graduates.

Additionally, women in developed countries vote 7-10% more than men, meaning that they are already the deciding factor at the polls. And yet in 2017, only 6.4% of the CEOs in the Fortune 500 list are women – though on average they earn more than their male peers. That must be because they are better!

The Power of Parity, a 2015 report by McKinsey & Company, concluded that best-in-class practices with regard to gender equality would add another \$12 trillion, or 10%, to global GDP through 2025. And if we had true equality, it would net a total an economic windfall of \$28 trillion, or about a full year of US' and China's combined GDP.

Change is coming – not because it is “fair”, but for the practical reason that women realising their desired potential is the last way left to grow the pie without growing the population in our low-productivity and aging developed economies.

Perhaps the trigger for all of this was the rediscovery in 2017 of the gross harassment women deal with every day when knuckle-dragging alpha males run the show. In 2018, the chauvinist old boys' clubs are shaken to their core by shareholders and enlightened self-reflective purges and **a woman occupies the top spot at more than 60 Fortune 500 companies by the end of the year.**



NON-INDEPENDENT INVESTMENT RESEARCH DISCLAIMER

This investment research has not been prepared in accordance with legal requirements designed to promote the independence of investment research. Further it is not subject to any prohibition on dealing ahead of the dissemination of investment research. Saxo Bank, its affiliates or staff, may perform services for, solicit business from, hold long or short positions in, or otherwise be interested in the investments (including derivatives), of any issuer mentioned herein.

None of the information contained herein constitutes an offer (or solicitation of an offer) to buy or sell any currency, product or financial instrument, to make any investment, or to participate in any particular trading strategy.

This material is produced for marketing and/or informational purposes only and Saxo Bank A/S and its owners, subsidiaries and affiliates whether acting directly or through branch offices ("Saxo Bank") make no representation or warranty, and assume no liability, for the accuracy or completeness of the information provided herein. In providing this material Saxo Bank has not taken into account any particular recipient's investment objectives, special investment goals, financial situation, and specific needs and demands and nothing herein is intended as a recommendation for any recipient to invest or divest in a particular manner and Saxo Bank assumes no liability for any recipient sustaining a loss from trading in accordance with a perceived recommendation. All investments entail a risk and may result in both profits and losses. In particular investments in leveraged products, such as but not limited to foreign exchange, derivatives and commodities can be very speculative and profits and losses may fluctuate both violently and rapidly. Speculative trading is not suitable for all investors and all recipients should carefully consider their financial situation and consult financial advisor(s) in order to understand the risks involved and ensure the suitability of their situation prior to making any investment, divestment or entering into any transaction. Any mentioning herein, if any, of any risk may not be, and should not be considered to be, neither a comprehensive disclosure or risks nor a comprehensive

description such risks. Any expression of opinion may be personal to the author and may not reflect the opinion of Saxo Bank and all expressions of opinion are subject to change without notice (neither prior nor subsequent).

This communication refers to past performance. Past performance is not a reliable indicator of future performance. Indications of past performance displayed on this communication will not necessarily be repeated in the future. No representation is being made that any investment will or is likely to achieve profits or losses similar to those achieved in the past, or that significant losses will be avoided.

Statements contained on this communication that are not historical facts and which may be simulated past performance or future performance data are based on current expectations, estimates, projections, opinions and beliefs of the Saxo Bank Group. Such statements involve known and unknown risks, uncertainties and other factors, and undue reliance should not be placed thereon. Additionally, this communication may contain 'forward-looking statements'. Actual events or results or actual performance may differ materially from those reflected or contemplated in such forward-looking statements.

This material is confidential and should not be copied, distributed, published or reproduced in whole or in part or disclosed by recipients to any other person.

Any information or opinions in this material are not intended for distribution to, or use by, any person in any jurisdiction or country where such distribution or use would be unlawful. The information in this document is not directed at or intended for "US Persons" within the meaning of the United States Securities Act of 1933, as amended and the United States Securities Exchange Act of 1934, as amended.

This disclaimer is subject to Saxo Bank's Full Disclaimer available at www.home.saxo/disclaimer

