



Theme #4: – Swiss NOK'd-out

We can think of three reasons to go short CHF/NOK.

1. The relative cycle is supportive of rate differentials. Inflation is at a much higher starting point in Norway than in Switzerland, leaving the Norges Bank much less room to manoeuvre than the SNB in the event of upside surprises to import prices or stronger European growth. Market pricing in Norway has evolved rapidly from three months ago, with the first hike now expected in Q3 2015 rather than Q1 2014, more or less in line with the Norges' own projections. NOK is also much better placed to benefit from a stronger US cycle with one of the strongest correlations to US growth, and CHF one of the weakest. One risk is house prices, which have risen precipitately in Norway over the last five years, a sharp reversal of which could weigh on domestic demand and prompt Norges' dovishness. We think the risks of this are slim, however, (see theme #6), and moderate falls will be welcomed by the central bank as skimming froth from the market.

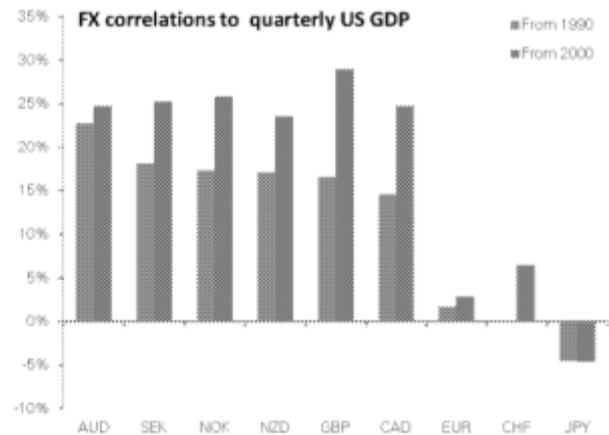
2. Swiss safe-haven unwind should follow Norway's. Like Switzerland, Norway experienced large-scale safe haven inflows as a consequence of the financial crisis, helping to pause customary current account surplus recycling. In the latter's case, these inflows have largely reversed, to the tune of NOK 190bn on a 2y/2y basis). This has been one of the primary recent drags on the krone, but appears to have largely run its course, in contrast to Switzerland where it has yet to begin.

3. CHF also more vulnerable to domestic outflows. As well as the foreign inflow, Norway and Switzerland both saw significant repatriation of domestic assets from abroad. Again, this flow has long turned in Norway but not yet in Switzerland. One possible catalyst will be stronger price pressures next year on the back of more robust growth. This should erode real returns Swiss domestics have enjoyed on already some of the most expensive assets in the world. Historically, Swiss capital flows have been counter-cyclically related to prices (chart 3). Indeed, CHF performance closely tracked changes in real yields last year. By contrast, while conventional Norwegian outflows have resumed, NOK is more protected by surplus savings being invested by the oil fund.

Along with the above, CHF/NOK appears fundamentally misaligned with traditional drivers like oil/gold. Finally, the trade benefits from being USD and EUR/USD neutral (with a 15 year correlation of 16% and -11% respectively).

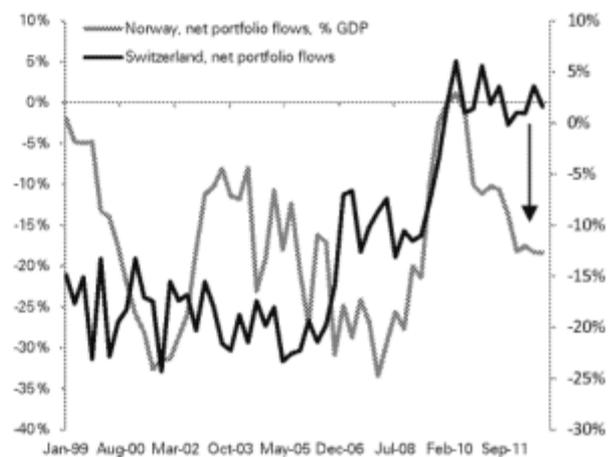
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NOK one of highest betas to US cycle, CHF lowest



Source: Deutsche Bank, Bloomberg Finance LP

Norway flow reversal nearly done, Swiss yet to begin



Source: Deutsche Bank, Bloomberg Finance LP

More Swiss inflation means CHF weakness



Source: Deutsche Bank, Bloomberg Finance LP