AM FX

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This guy can't talk, he's a little horse.

It's hard to explain puns to kleptomaniacs because they always take things, literally.

Thx RBrand

Current Trades

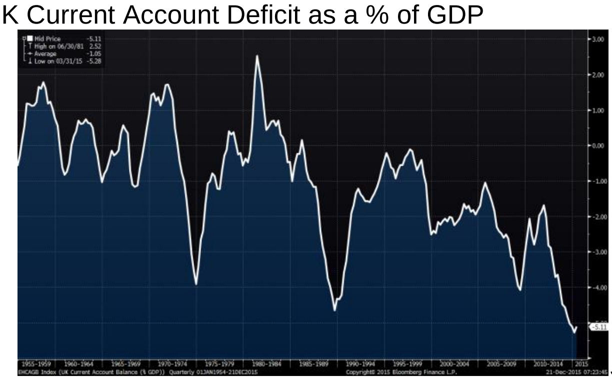
Pricing up bearish GBP strategies for 2016

Reasons to hate the pound

There are a lot of reasons to hate the Great British Pound into 2016:

1. **Very large current account deficit**. The UK runs a big negative balance and has been doing so for a few years. These liabilities have most likely been financed by inflows from the Middle East, Russia and China and so GBP has held in OK as the market positioned for a UK rate hike. It is not controversial to suggest that financial flows from the Middle East, Russia and China are drying up substantially now and so the worst UK Current Account deficit since at least 1955[1] may come home to roost for the pound in 2016. Current Account balances are tricky for FX trading because they only matter when they matter; but I have a feeling this one will matter in '16.

Chart1: UK Current Account Deficit as a % of GDP



Source: Bloomberg

2. **Brexit nerves**. There is still uncertainty around the timing and nature of any referendum but the Brexit story should cast a shadow in 2016. The timing of the vote is unknowable but mid-year 2016 seems fairly high delta. Bookmaker odds suggest something around a 40/60 split with the "stay" outcome in the lead.

3. **UK monetary policy has decoupled from the US, finally**. For most of 2015, EURGBP traded like a EURUSD proxy as ECB easing meant lower EUR and Fed hikes meant Bank of England hikes coming soon. This all changed after the last inflation report as Mark Carney broke the link between the Fed and the BoE and showed UK monetary policy is more Europe than America. Carney has a strong bias to do nothing and there is no smoking gun for a UK hike so they could stay dovish all year. It will also get more difficult to hike as the Brexit vote nears so odds of an on hold BoE increase over time.

How to play it: There are a lot of ways to play it: Buy GBPUSD put spreads, go long EURGBP cash, sell GBPCAD topside, sell GBPJPY topside.. Or do all four. My preference would be to do a basket of all four of these ideas so that you are diversified and not subject to too much concentration risk in either a specific currency or long or short vol. If you need a price: I hear Citibank is pretty good in FX options.

Good Luck ↕ Be Nimble

[1] Bloomberg data goes back to 1955

IMPORTANT DISCLOSURES

Contact:
https://icg.citi.com/data/documents/S&T_ExternalDiscl_0209.pdf

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