**WHY SHOULD YOU BE BUYING CHF?**

* CHF is still considered as a safe haven
* There are number of political risk-off events in the near term future
* The inflation continues moving well below SNB’s target….
* ….but strong built up in FX reserves suggest SNB is approaching its purchasing limits

**CHF is still considered as a safe haven**

The ongoing CHF appreciation pressures continue to be a major issue for the Swiss central bank. Indeed, investors continue to be in search of franc in the periods of increased uncertainty like last year’s Brexit and Trump’s election victory or this year’s worries about Trump’s politics. Beside that, the franc continues to be under pressure from the ECB’s expansionary monetary policy that will last at least by this year end. In such circumstances and despite negative interest rates, sight deposits that Swiss banks keep at the SNB continue to increase and amounted more than 70% of GDP at the 2016 year end (see graph below).

**There are number of political risk-off events in the near term future**

As said, both Brexit and especially American elections led to the increased appreciation pressure on franc. I see markets at least through the course of first half of 2017 largely driven by politics events. Namely, French elections are scheduled for the end of April where Marine le Pen is gaining popularity and will likely head toward the second round. While chances are low, if le Pen indeed wins the consequences will be surpassing France borders and potentially having a strong impact on the future of the euro zone given le Pen’s anti EU stance. Furthermore, anti-EU parties are also gaining popularity in Netherlands where elections are scheduled for the mid-March and German is facing a similar problem as well. Italy has yet to define its election law that will likely increase what is already considered as high political instability in the country. Moreover, Catalonia is getting ready for the independence referendum at the latest in September. While markets seem to have forgotten about Greece for some time, EUR7.4bn of maturing debt only in first half of 2017 will certainly remind them. Greece has not yet managed to accomplish deal with its creditor and has not fulfilled required reforms suggesting little scope for debt forgiveness or delay. The latter will be discussed at this week Eurogroup meeting in Brusseles.

**The inflation continues moving well below SNB’s target….**

The SNB’s ultra expansionary monetary policy seem to have impact on the real economy. Indeed, lending is currently expanding in the 2%-2.5% yoy region while overall economy grew at 1.5% in 2016 thus being in line with the euro zone and US. However, while increasing slightly in the recent period, inflation continues to move below zero and significantly below SNB’s 2% mid-target. Therefore the SNB continues to consider franc as overvalued and hopes it would depreciate over time. The evidence of the latter can be seen in SNB’s governor Jordan statements where he continues to emphasize SNB’s willingness to stay active on the market if required.

**….but strong built up in FX reserves suggest SNB is approaching its purchasing limits**

While SNB would like for franc to depreciate it seems to have a limited scope of ammunition to do so. The deposit rate lowering to -0.75% seem to have reached its limit with SNB keeping the rate unchanged in spite of continued appreciation pressures. Since January 2015 when rate was lowered not only that franc has not maintained sustainable depreciation but also inched higher in the recent period. In my view, the SNB refrains from further interest rates lowering as they would probably have a minimum or non expansionary effects on the economy.

That said, it seems that FX interventions are staying the only SNB’s tool against the backdrop of strong franc. However, let’s remember that SNB’s has once already abandoned the floor as they were considered about the balance sheet strong increase. Since roughly 80% of GDP in January 2015 when the floor was abandoned, the FX reserves increased to more than 105% OF GDP in the end of 2016 while franc appreciated in spite of that.

All in all, ongoing risk-off events will certainly increase investors search for safe haven at least in the short term. At the same time the SNB is clearly reaching its balance sheet expansion limits and has already allowed franc to inch slightly higher in the recent period. The FX interventions at the current pace are not sustainable and franc is thus set to appreciate further.