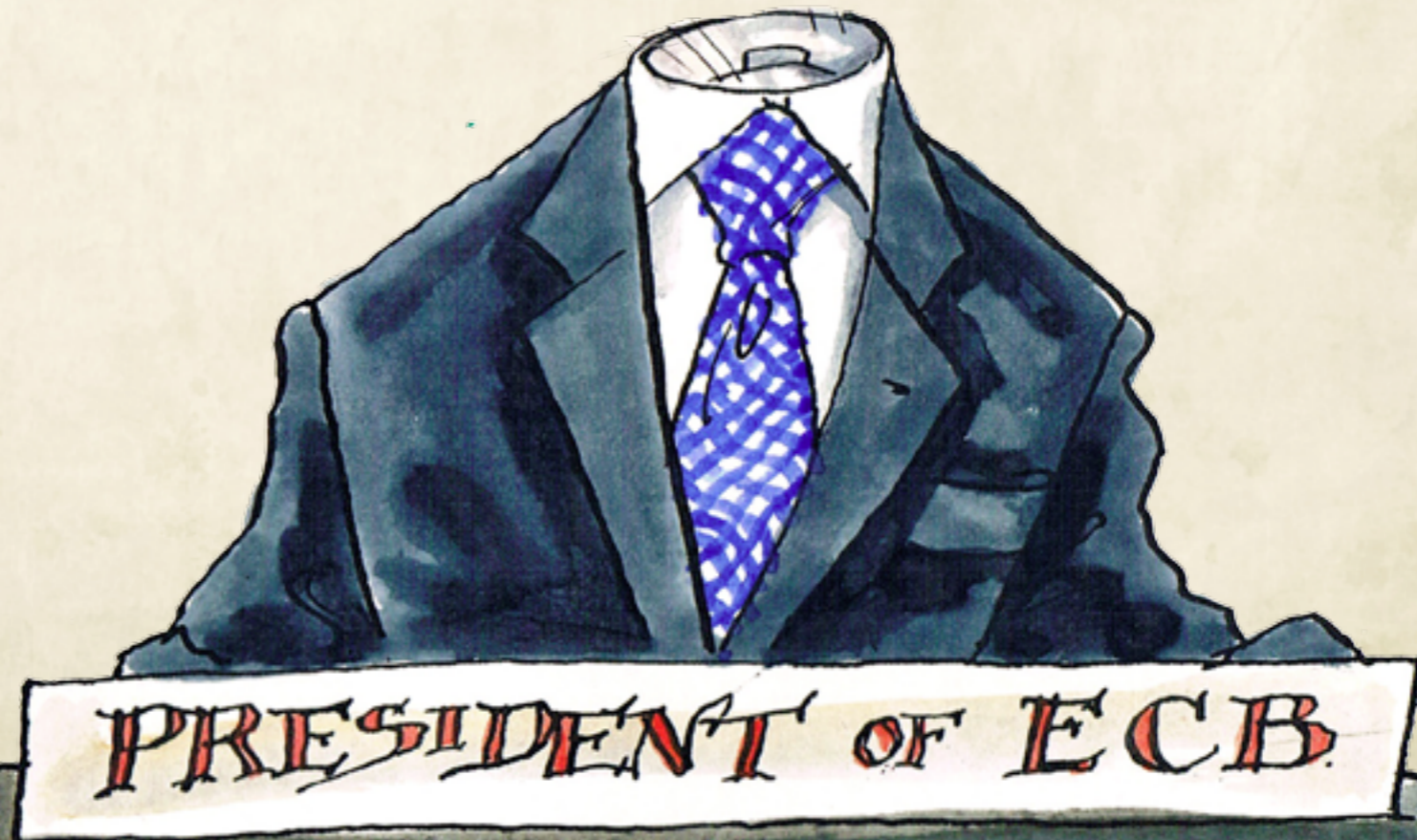


SAXO
GROUP

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Saxo Bank presents

OUTRAGEOUS PREDICTIONS for 2015





A reckoning's coming

STANDING ON THE doorstep to 2015, we are experiencing near perfect conditions for momentum and equity investment. Inflation has fallen to its lowest since the 1980s, interest rates have followed, and energy is relatively stable.

Corrected for inflation, oil at \$65/barrel today equals \$20-40/b in the 1970s.

Low volatility has given investors a false sense of security that could lead to the biggest upset in 2015. Central bankers meanwhile have become the generals in an economic war in which the final tool in the box - competitive currency devaluations – merely exports problems overseas.

Nowhere exemplifies this better than Japan after the latest bazooka launch by Shinzo Abe threatens to become an out-of-control, infla-

tion-stoking missile. Japan may have bought the global markets a further quarter or two of protection but the real world will have its say.

We saw it for one week of mayhem in October. If that's anything to go by, we are in for a rollercoaster ride in 2015. Tangible assets and production sit at all-time lows.

Paper money investment has crowded out productive capital while societies are dominated by hairdressers and bankers. We're losing the art of manufacturing.

Meanwhile the power of the US of A is waning as China rises and when the superpower pecking order changes, volatility and war ensue. Nothing is ever given and Outrageous Predictions remains an exercise in finding ten relatively controversial and unrelated ideas which

could turn your investment world upside.

By imagining the most negative scenarios and events you will have a better chance of navigating the turmoil, be it a Russian default, volcanoes spreading havoc, or an internet Armageddon.

And we at Saxo Bank remains convinced higher volatility and a potential move towards a mandate for change is upon us as macro thinking enters a final fight to the death before we can again put our faith in people, ideas, education and change rather than hollow promises. 2015 will be a tough year but potentially also the year we look back at as the nadir.

As Winston Churchill famously said:

"If you are going through hell, keep going".

STEEN JAKOBSEN

Chief Economist, Saxo Bank



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• Illustrations by **Chris Burke**




Russia defaults again



SAXO BANK REMAINS a great believer in Russia's potential long-term situation, but the country's economy was heading for recession and current account deficits even before sanctions, the 25% drop in oil prices and the conflict with Ukraine.

These problems have now become a near-emergency, and nowhere is this better illustrated than by the ruble and its 40% drop (versus the US dollar) this year.

There is a perfect storm brewing for the Russian economy that could either end with government-owned companies or with the government itself selectively moving into a default. This may be part of an escalation between Russia and the EU/US or it could be driven by lack of access to funding.

Russian companies need to repay \$134 billion in debt between 2014 and end of 2015. This, of course, is backed by currency reserves of \$400 billion. Although this may buy Russia some time, the Rotenberg law (repaying lost money from sanctions to Russia business owners), the ruble intervention, an incoming current account deficit, big budget deficits (lack of tax and oil revenues), and close to no access to financing from capital markets means that this \$400 billion could become petty cash.

Russia already has long-term discounted values in energy, mining, its companies, and its people. Consequently, a new start (as in 1998) could be what's needed for the country's future, but it also needs a diplomatic solution regarding Ukraine. 

  Watch **Steen Jakobsen** talk about his Outrageous Prediction on TradingFloor.com



“ There is a perfect storm brewing for the Russian economy that could end ... with the government itself selectively moving into a default ”



Volcano eruption decimates crops

IN 2015, the already-active Icelandic volcano Bardarbunga erupts, leading to an unprecedented, further release of noxious sulphur dioxide gases that cloud skies over Europe. The eruption shifts weather patterns, lowering world grain output and leading to the doubling of grain prices.

Fortunately, the sharp increase is only partially due to actual declines in grain harvests, and mostly stems from the fear generated by this event as less food-secure nations scramble to stock up on supplies.

No one is talking about the Icelandic volcano Bardarbunga, yet this volcano is responsible for the largest volcanic eruption of the last 10,000 year.

Bardarbunga has been “quietly” erupting nonstop since the end of August, with little attention except for scenic drone flyovers as the eruption is not explosive, but magmatic.

Still, with more than a cubic kilometre of erupted lava it is already the largest lava eruption in Iceland since the Laki fissure eruption of 1783-4, which released an estimated 14 cubic kilometers of lava and clouded Western European skies with toxic sulphur dioxide emissions.

These emissions, just to note, likely contributed to poor wheat harvests across Europe, and thus to the French bread shortage that helped feed the events leading to the French Revolution.


So far, the eruption has been confined to a large long gash, or fissure, that has opened up adjacent to Bardarbunga itself at Hohluraun and created a lake of lava that measured over 70 square kilometres as of mid-November.

The eruption is emitting more sulphur dioxide than all of Europe’s industry combined.

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Meanwhile, constant earthquake swarms are being recorded across the enormous, sub-glacial caldera of Bardarbunga itself, which at nearly 80 square kilometers is almost as large as the island of Manhattan.

The caldera is rapidly subsiding and risks collapsing as the magma under the volcano pours out of the nearby fissure at Hohluraun.

A collapse could lead to a far more intense eruption phase with potentially climate-altering consequences for the next year or more. 

“ The eruption is emitting more sulphur dioxide than all of Europe’s industry combined ”



Japanese inflation to hit 5%

NOBODY HAS MORE experience with various monetary easing schemes than the Bank of Japan, but despite several decades of little to no success, the central bank continues to pile on like an addict in need of his next fix.

And like an addict, more and more is needed to maintain the same effect.

Predictably then, the monetary shaft of prime minister Abe's three arrows have failed to do much to revive the economy, growth forecasts for 2014-16 have been revised down

and inflation has begun to slide again.

Indeed, the latter will take a further hit when the one-year anniversary of the 2014 VAT hike comes around, worsening demographics add to deflationary pressures, and real household incomes fall outright despite a tight labour market.

Against this backdrop, we see an outside chance of inflation spiking to at least 5% next year in Japan, and that is without incorporating another VAT hike into our scenario.




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“ **The central bank continues to pile on like an addict** ”

The incessant money printing by a progressively more and more dovish BoJ, which at the going rate will buy around 60% of any new government bond issues, not to mention equities and other assets, will fuel asset prices and in turn price pressures.

The continuing slide of the yen against other major currencies, notably the US dollar and the euro, pushes up prices of foreign goods and services, which will add to inflation over the coming quarters.

And the slide may be far from over as foreign investors flee Japanese assets in anticipation of further monetary stimulus, yet another upside risk to inflation.

Therefore, we outrageously predict that inflation will top 5% in Japan next year. 





Draghi quits ECB

MARIO DRAGHI'S TERM as president of the European Central Bank is far from over but his time at the ECB may be limited if the recent spate of noise and leaks is the new reality at the central bank.

Draghi has probably reached the limit on how much he can do merely by “talking to the market”.

It's generally assumed that the European economy now is so weak that ECB quantitative easing is almost a given.

But Draghi might have to leave the scene in order to get that programme off the ground.

This is almost Game Theory: Draghi has reached his limit while back home in Italy President Napolitano wants to be out of office no later than June 2015.

Prime Minister Renzi, who runs a minority government, needs a broadly accepted figure to replace the popular, ageing president as the Italian parliament needs to back the candidate by a two-thirds majority.

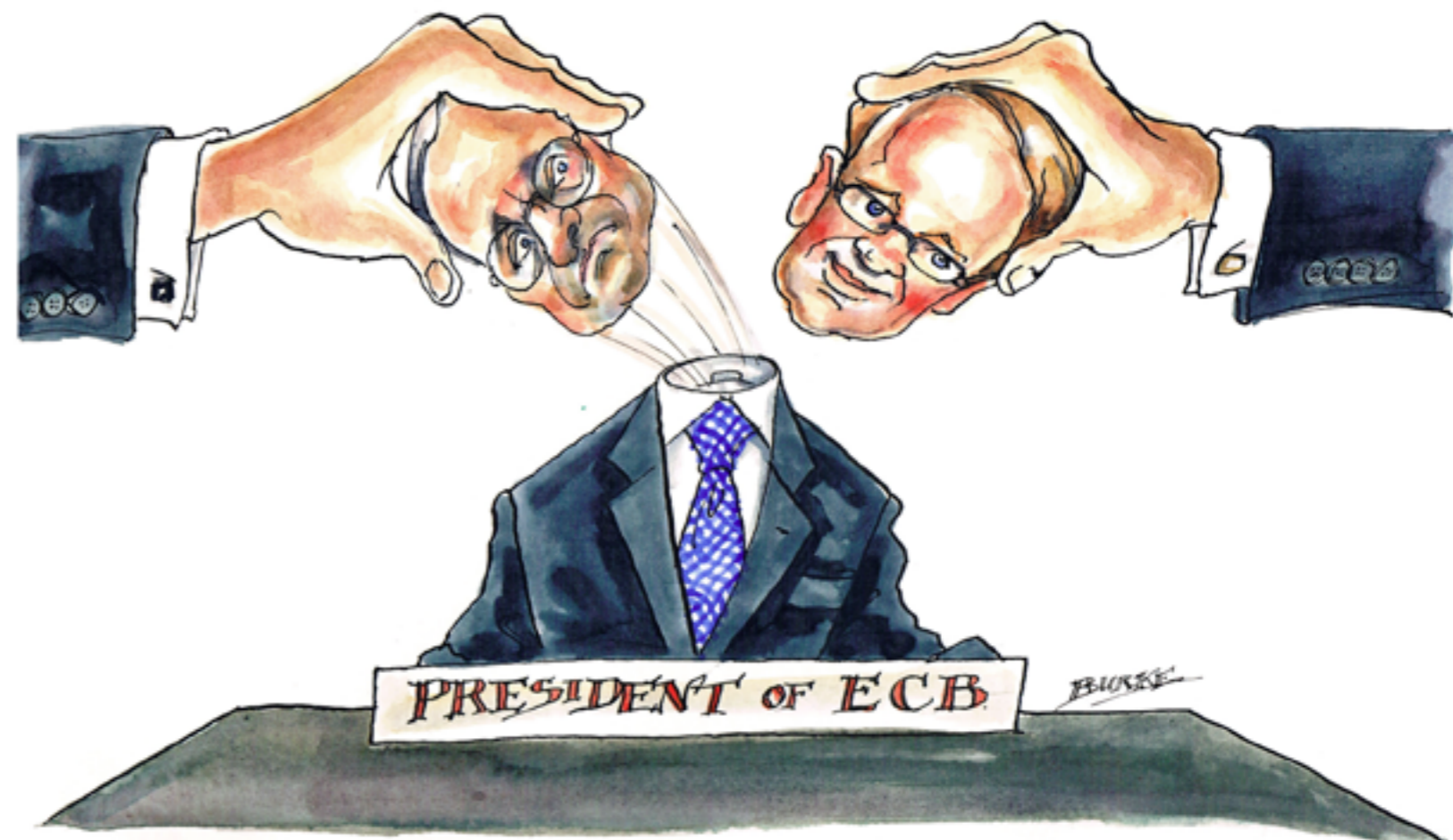
Could the real surprise next year be that Renzi and Napolitano ask Draghi to come home to save the reform process and secure a broad mandate to finally move Italy forward, and that Jens Weidmann takes over the ECB presidency in a quid pro quo deal that sees Bundesbank/Germany allowing a QE-light programme to go ahead under the supervision of a German president and not a Club Med member?

Politics is the art of compromise and this compromise may be exactly what is needed for Europe to embrace QE late – too late, but as they say in macro circles, imagine if we had not done it. **TF**

**TF**

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“ Draghi has probably reached the limit on how much he can do merely by talking to the market ”



Corporate bond spreads to double in 2015

IT HAS NOT BEEN Europe’s growth so as much as the actions of the European Central Bank that have driven down corporate bond yields in Europe. The yield on euro corporate non-investment grade bond has declined significantly since the peak in the fourth quarter of 2011.

In 2015, economic growth will slow down further pushing investors to question public policies.

While central banks are keeping sovereign and ABS-yields suppressed, the ECB will not be the saviour in European non-investment grade corporate bonds as its mandate does not reach

grade European corporate entities is the perfect reflection of the health of the European corporate bond sector.

It is thus our yardstick for measuring the development in non-investment grade European corporate bonds.

“ The party enjoyed in high yield credit is coming to an end as the ECB’s new policies fail to deliver growth ”

As an example, Royal Bank of Scotland’s yield on its subordinated euro-denominated 6.934% coupon maturing in April 2018 has declined from 13.6% on November 29, 2011 to 2.2% on November 17, 2014.

As a result, European non-investment grade corporate bonds are up 46% on a total return basis since the bottom on October 7, 2011 or 13% annualised.

However, the party enjoyed in high yield credit is coming to an end as the ECB’s new policies fail to deliver growth as monetary policies cannot offset the lack of private sector growth.

that far – the Bundesbank will simply not allow it.

With sentiment on high yields flip-flopping in 2015, investors are left finding sparse liquidity and steep prices in order to exit positions.

With an ultimate washout in high-yield credit, shock waves will once again shake the foundation of Europe’s weak economy.


The Market iTraxx Europe Crossover Index comprising of 75 equally weighted credit default swaps on the most liquid non-investment

The index is trading at around 350 basis points and our outrageous prediction is that the index will explode to at least 700 basis points as investors run for the exit. **TF**

  Watch **Peter Garnry** talk about his Outrageous Prediction on TradingFloor.com



Internet hacks smash online shopping


  Watch **John J Hardy** talk about his Outrageous Prediction on TradingFloor.com

THE LAST COUPLE of years have seen increasingly aggressive hacking activity of major corporations – from the relatively harmless, if high profile hacking of celebrities’ personal photos on Apple’s iCloud platform to major retailers like Target and Home Depot having millions of its customers’ credit card information exposed.

In 2014, we also saw the mighty JP Morgan compromised for months before the company even knew its systems had been breached. And five million Gmail account passwords showed up on a Russian website.

Such attacks require extraordinary sophistication and may even be state supported in retaliation for the US’ increasingly aggressive use of financial sanctions in its geopolitical confrontations around the world.


In 2015, new underhanded attacks on e-commerce’s largest players become even more widespread and increasingly aggressive.

Amazon.com, the largest e-commerce retailer and aggressive player in web-based services suffers a decline of 50% from an already egregious overvaluation and on a shift in sentiment as it suffers lower growth rates, even if it is not necessarily the victim of a hacking itself. 

“ Such attacks require extraordinary sophistication and may even be state supported ”



China devalues yuan 20%

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WITH THE CHINESE domestic housing and credit bubble finally correcting, if not imploding,

China will be looking for any way it can to ease the enormous deflationary pressures that characterise the downside of a credit cycle.

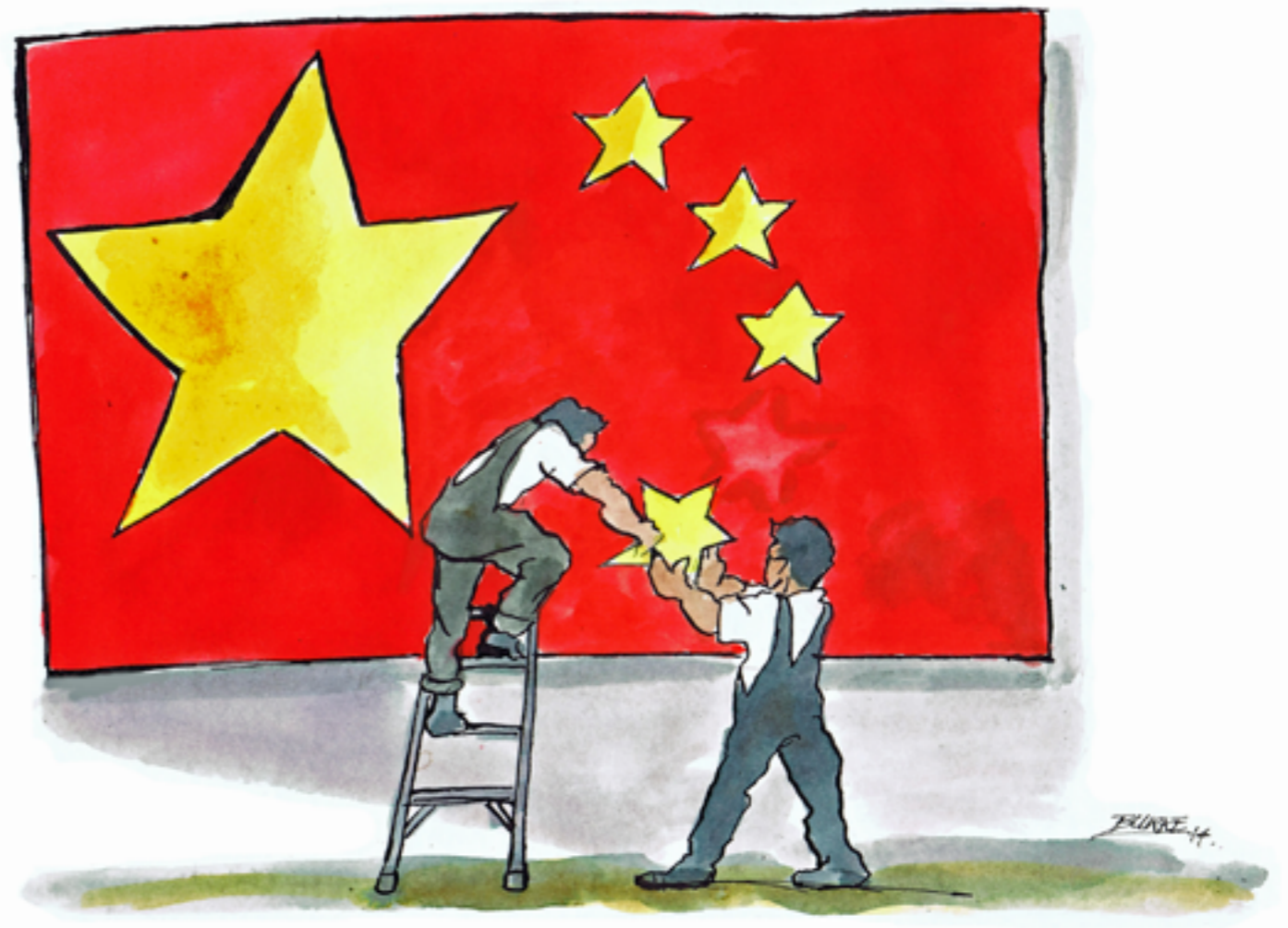
Aggravating the pressure on China to act are almost three consecutive years of producer price deflation driven by massive overcapacity.

A Chinese yuan at record highs (in inflation-adjusted terms) in this environment makes no sense, especially in light of its neighbour Japan's simultaneous record low exchange rate (also in inflation-adjusted terms as of mid-November).

So in 2015, China moves rapidly and persistently to devalue its currency over the course of the year, joining Japan and other countries in the global struggle to import inflation.

This sets off a chain of Asian devaluations and the risk of hostile trade and financial sanctions with Japan. 

“ China moves rapidly and persistently to devalue its currency over the course of the year ”



Cocoa futures hit USD 5,000/tonne

CHOC HORROR – who ate all the chocolate?

Demand for chocolate is rising globally as Western preferences shift towards darker chocolate and Asian appetite for the sweet stuff increases as economic growth propels more and more of them into the ranks of the middle classes.

The appetite for chocolate among Chinese consumers continues to rise but the estimated per capita annual consumption is still only 5 percent of what is eaten by a Western European consumer -- a clear indication that demand will only continue to rise over the coming years. The rising popularity of dark chocolate among traditional consumers in the US and Europe has also helped trigger a rise in demand.

Dark chocolate has a cocoa concentration of up to 70% compared with just 10% in an average milk chocolate bar.

Rising demand requires rising production, not least from the world's largest growing region in West Africa where Ivory Coast and Ghana account for up to 70% of global output.

A record production from Ivory Coast last year may be exceeded this year but despite this potentially bearish outlook cocoa futures continue to trade close to their five-year average.


In other words, it doesn't take much to rock the boat, a fact of which we were sharply reminded when cocoa suddenly spiked on concern about the Ebola virus earlier this year.

In order to meet the increased demand and to halt the growing imbalance between supply and demand, cocoa producers require near perfect growing conditions year after year.

“ Cocoa suddenly spiked on concern about the Ebola virus earlier this year ”

Underinvestment in West Africa has resulted in ageing trees not being replaced fast enough and this, combined with the precarious financial situation of many small farmers, makes regular outbreaks of black pod disease difficult to fight due to lack of cash for regular spraying.

We see the risk of the near-month cocoa futures reaching USD 5,000/tonne sometime during 2015.

This would represent a new record as it would exceed the previous record of USD 3,775/tonne that was reached in March 2011 when a civil war in Ivory Coast disrupted supplies. 



Watch **Ole Hansen** talk about his Outrageous Prediction on TradingFloor.com



UK house sector to crash

WHILE HOUSING MARKETS were crashing left and right around the globe in the lead-up to the global recession, the UK housing sector held up relatively well.


Though prices did drop by around 20%, that loss has already been recouped on a national level, and in London, prices have risen to a new all-time high this year, up more than 30% from the pre-recession 2007 peak.

Overall, the UK economy has rebounded much more admirably from the global recession than other major economies, notably continental Europe where the euro area is still struggling for growth. In comparison, economic output in the UK stands 3.4% above the 2007 peak aided by rising house prices.

The party may be about to end, however, for UK home owners. Not only are indices tracking house prices already looking much weaker than in the last couple of years – including star performer London – but there are other reasons to fear an impending crash in the UK housing market.

The Bank of England is moving closer to its first rate hike since 2007, which will put upward pressure on mortgage rates and in turn household finances already undermined by weak wage formation.

Furthermore, the quick rebound in house prices may induce a wave of selling from ordinary households still struggling to make ends meet, especially in pricier neighbourhoods of London where affordability has gone down the drain as prices have surged, and with both private and public debt remain high implying low manoeuvrability when and if prices start to head south.

Therefore, we outrageously predict the UK to experience a housing crash with prices falling as much as 25% in 2015. 





Watch **Mads Koefoed** talk about his Outrageous Prediction on TradingFloor.com

“ **The quick rebound in house prices may induce a wave of selling from ordinary households** ”



Brexit in 2017


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THE UK INDEPENDENCE PARTY wins 25% of the national vote in Britain's general election on 7 May, 2015, sensationally becoming the third largest party in parliament.

However, because of the UK's first past the post system, whereby a party must come first in a constituency in order to win the sole parliamentary seat, UKIP secures only a third of the seats of both the Conservatives and Labour.

Nevertheless, UKIP, which campaigns on an anti-EU, anti-immigration ticket, holds the balance of power and joins David Cameron's Conservatives in a coalition government.

Its leader, Nigel Farage, becomes deputy prime minister and Cameron calls for the planned referendum on Britain's membership of the EU in 2017.

Gilt yields increase sharply as opinion polls suggest the majority of the British people will vote to withdraw from the European Union completely given the chance. This sets up our Outrageous Prediction of the UK leaving the EU in 2017. 

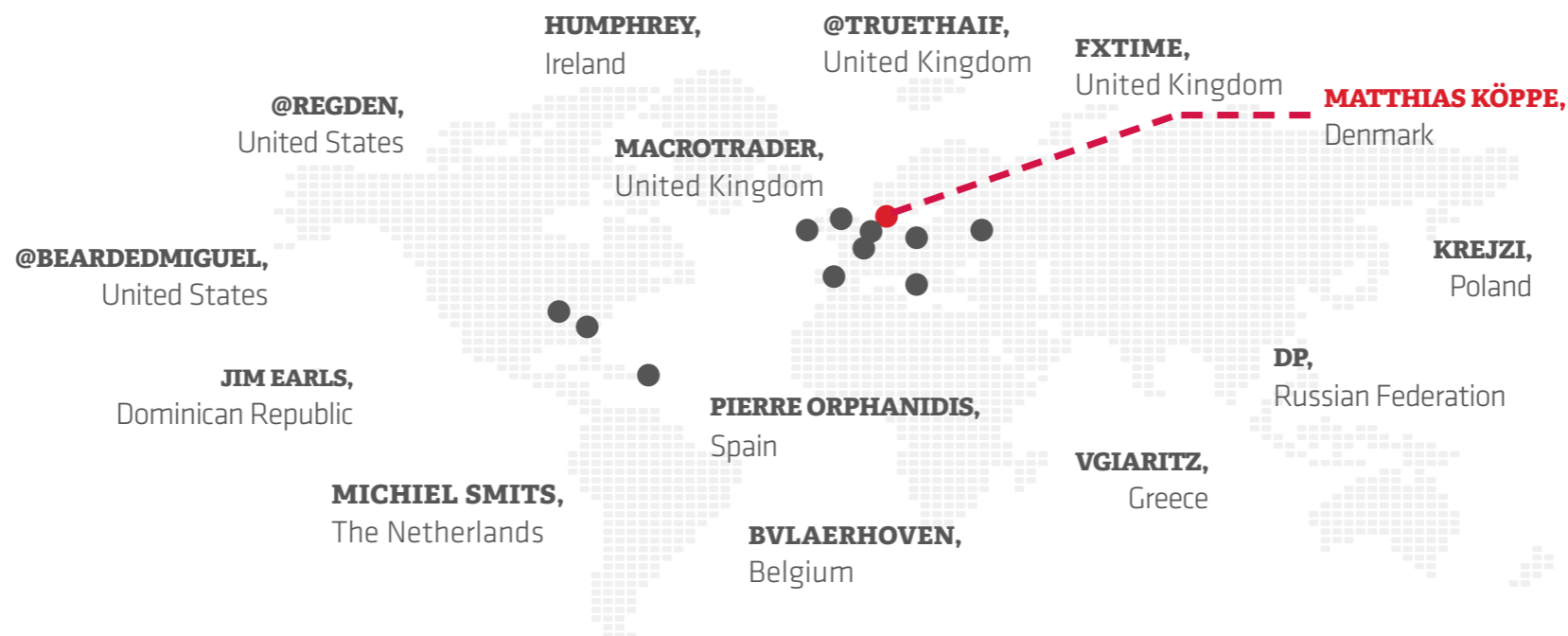


“ Gilt yields increase sharply as opinion polls suggest the majority of the British people will vote to withdraw from the European Union ”





The best predictions from the community



WINNING PREDICTION BY MATTHIAS KÖPPE:
Capitalism evolves to version 2.0! Sharing economy takes over. Buy installing platforms like Uber, AirBnb or services like crowd-funding, prices for diverse products and services decrease under the image of a more sustainable development; the major reason is hidden behind that movement.

To overtake already established systems and markets by dictating new rules, sling out labor rights, collect consumer data and generate profits for unknown investors. A shift of who has the power to decide! The border between social/sustainable initiatives and profit maximising investments will float.

Lets see if society realises that potential of change.

MICHIEL SMITS:
 My outrageous prediction is that in at least one Eurozone country the government will fall and the establishment will lose control in subsequent elections, thus putting the Euro experiment on the brink of collapse. Europe is being endangered, for a long time already, by just those people that really want it so desperately!

MACROTRADER:
 Apple will create The Apple Bank from its cash hoard, with the goal of ApplePay replacing credit card companies

BVLAERHOVEN:
 Japan completely loses the economic pedals and prints negative GDP's for all 4 quarters. US-DJPY closing in on 150.00 2. Gold moving higher towards 1600 on repatriation moves from central banks.

JIM EARLS:
 U.S. 30 Yr. Bond will yield under 2% by the end of 2015.

HUMPHREY:
 €1 = \$1, USA rates begin to rise earlier than expected and Dragi gets the go ahead to aggressively buy Bonds to keep Germany/EU out of recession

VGIARITZ:
 Greece the best performing market in the world. Athens general above 1550, now at 970. EurUSD 1.

DP:
 My outrageous prediction for 2015 consists in the first usage of tactical nuclear weapon since 1945

KREJZI:
 Putin is overthrown and replaced by more hawkish leader.

@REGDEN:
 Amazon buys Twitter to target ads, individualized deals and order taking #2015OP

@BEARDEDMIGUEL:
 A major Chinese Internet company is exposed as a fraud causing a plunge in the sector & leading to a hedge fund ice age. #2015OP

FXTIME:
 Gold reaches \$2500 as Russia invades Estonia and Latvia.

@TRUETHAIF:
 Argentina to use corned beef as their currency standard. UK bans sick pay to assist big business. France to privatise Belgium #2015OP

MACROTRADER:
 Sudden reversal of Abenomics in Japan resulting in a rapid fall of USDJPY all the way back to 90.

Huge long positions are stopped out in this process.

PIERRE ORPHANIDIS:
 France plunges into a Greek-style crisis. The yield on French 10-year bonds jumps to 15%. Italy's, Spain's, Portugal's and Greece's yields on 10-year bonds skyrocket to 30-40%.





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