MacroResearchBoard
mrb partners **FOREIGN EXCHANGE**
Independent Investment Strategy

November 25, 2016

# Currencies Navigate Growth Vs Protectionism

We had noted that the U.S. dollar would appreciate regardless of the outcome of the U.S. election, which has been a winning position. That said, the outlook for most other currencies (and the dollar longer term) will be heavily influenced by the competing forces of stronger global growth and the push towards protectionist policies. We find it most useful to begin by dissecting and independently assessing the impact of these forces when determining currency strategy.

### *Stronger Global Growth Absent Policy Mistakes*

The global economy has been stronger than most investors acknowledged and should continue to improve, with all of the "three-legged stool" contributing (**chart 1**):

- The U.S. has been in a durable economic recovery for several years. The job engine has been incredibly steady and wage growth slowly edging up. At the same time, deleveraging pressures are fading and household sector credit (including mortgage lending) is picking up. In turn, the economy will gradually shift from what we have characterized as being "subdued" to a more "normal" economic expansion, bolstering investor confidence and dealing a blow to proponents of the secular stagnation thesis[1]. The Trump-led government will push for a fiscal

[1] MRB *Theme Report*, "*The Long-Term Rate Outlook (Part I): Secular Stagnation Versus MRB's "Aftershock" Theory*", October 18, 2016

**MRB Foreign Exchange Recommendations***

vs USD ■ vs EUR □

| | – | | N | | + | Page |
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* 6-12 month horizon
Note: + = maximum overweight, N = neutral and – = maximum underweight

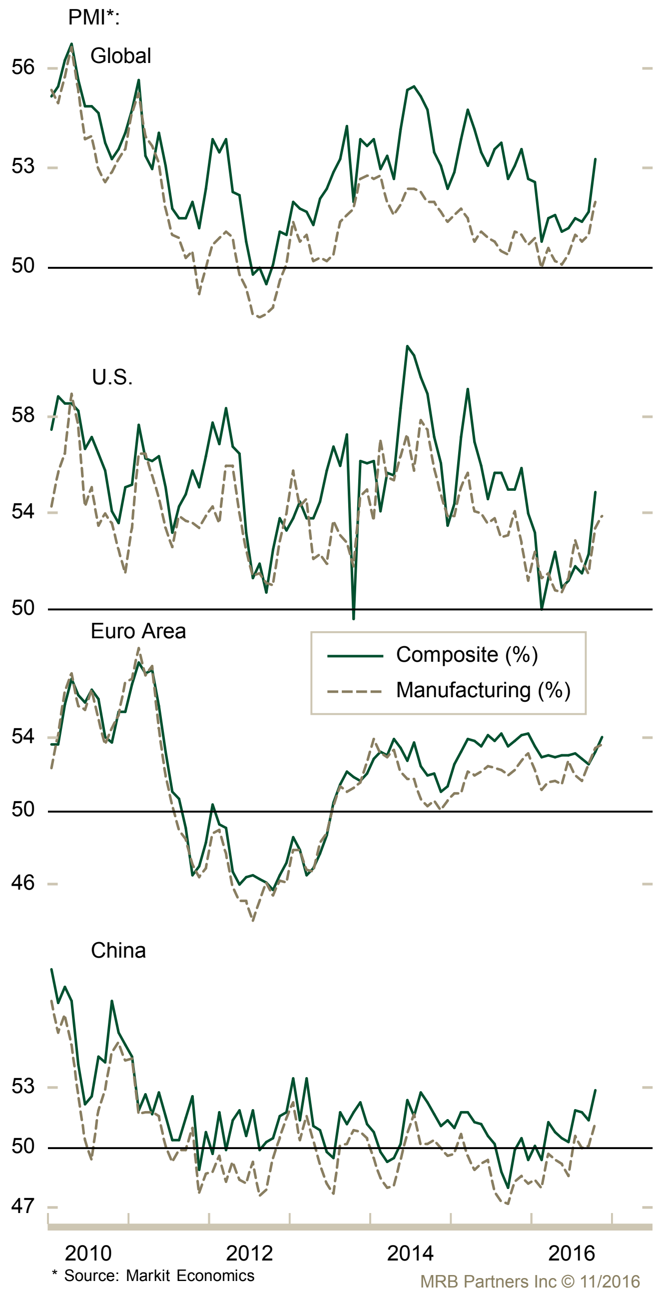


- The U.S. dollar is somewhat overvalued and overbought, but still represents the best risk/reward tradeoff until political clouds clear.
- Euro area growth is stronger than investors acknowledge, but the euro will be weighed down by upcoming elections and easy ECB policy.
- The Swiss franc serves as a hedge against greater political uncertainty in the U.S. and Europe.
- Stay cautious on currencies in export-oriented economies for now. Many of these currencies are cheap and some are appealing (primarily non-commodity countries), but will only strengthen ***if*** the global push towards protectionism fades and trade strengthens.
- Stay short the yen and do not bottom fish the pound.

stimulus package, which should help reinforce the existing tailwinds.

- The euro area economy is transitioning into a self-reinforcing expansion. In many regards the euro area looks like the U.S. economy 3-4 years ago[2]. As was the case with the U.S., investors are underappreciating the resilience of the regional economy. A very accommodative monetary policy setting and a steady job engine will ease the deleveraging adjustment and should support an ongoing expansion.
- The Chinese economy has reaccelerated this year on the back of previous stimulus measures. In fact, the housing market is running hotter than the authorities would like, which has now encouraged increased macroprudential tightening[3]. This poses a potential threat of a slowdown at some point in 2017, but conditions should remain supportive for the time being.

Chart 1 **The "Three-Legged Stool" Is Contributing To Global Growth**




In this backdrop, the U.S. dollar should appreciate due to a strengthening U.S. economy and the resumption of the Fed rate cycle (i.e. both relative growth and interest rate differentials will slowly work in favor of the dollar). Although U.S. fiscal stimulus will result in larger government deficits, investors are unlikely to fixate on this longer-term risk over the next year. That said, the U.S. dollar upleg (in this environment) should be gradual. The reason is that the currency is already pricey and the euro area economy will positively surprise investors, limiting downside for the euro.

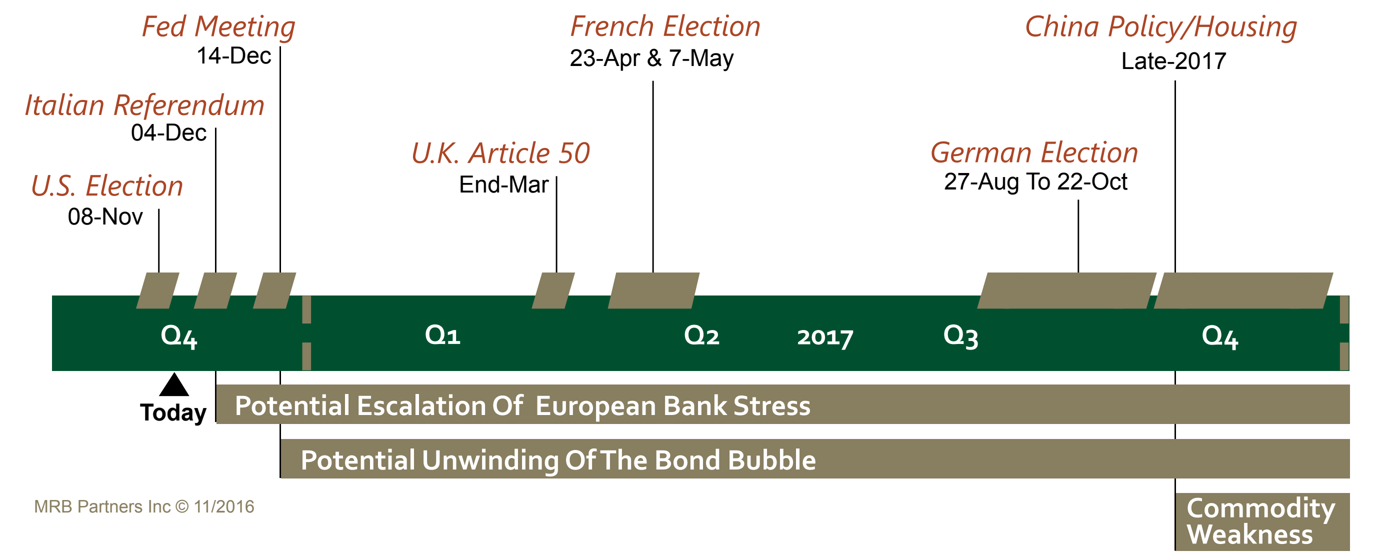
Moreover, with all three global growth engines (i.e. the U.S., euro area and China) in solid shape, global trade is likely to pick up at least modestly. In turn, currencies in export-oriented economies should find support from what are cheap levels. Among these, we would favor the non-commodity currencies as the recent bounce in natural resource prices is likely to fade. Still, better global demand will offset some of the oversupply and prevent commodity prices and related currencies from falling sharply.

Global growth conditions are strengthening

[2] Note that MRB will soon publish a research report on this topic to complement our other research on the euro area.

[3] **MRB *Theme Report***, "***How China's Property Boom Goes Bust (Again)***", October 11, 2016

Chart 2 **Timeline Of Political And Economic Risks**




### *Overlaying Protectionism*

The offset to this pro-growth backdrop is the potential for isolationist policies in a few key governments. We have outlined the forces driving political instability, the misguided push for protectionism, and the adverse consequences in several recent **MRB *Theme Reports***[4]. These policies could cause significant damage to the global economy and create tremendous investor uncertainty if enacted (**chart 2**). Most notable are:

- The U.K. is on schedule to invoke Article 50 and begin Brexit negotiations by the end of March. Ideally, these negotiations will be dragged out, as a "hard" Brexit would not only be damaging for the U.K. economy but could create material financial contagion risks, especially for the euro area[5].

Protectionist policies would be a mistake

- U.S. voters just elected Donald Trump with an anti-trade and anti-immigration platform. There is a reasonable chance he will back away from his campaign promises and merely try to get a couple of insignificant, but symbolic, wins[6]. If instead Trump pushes ahead with meaningful isolationist policies, then this would be stagflationary for the U.S. and deflationary for the rest of the globe.

- There are several important euro area political events on the horizon over the next several months, including the Italian referendum and elections in France and

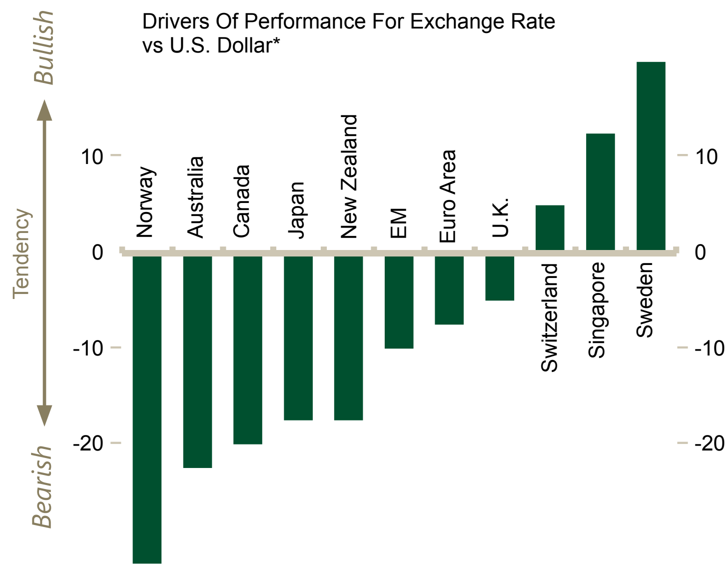
[4] **MRB *Theme Reports***, "*A Perfect Storm For Political Instability (Part I)*", September 27, 2016, **MRB *Theme Reports***, "*A Perfect Storm For Political Instability (Part II)*", September 28, 2016, **MRB *Theme Reports***, "*Forced De-Globalization (Part I): Benefits And Costs Of Trade*", November 8, 2016 and **MRB *Theme Reports***, "*Forced De-Globalization (Part II): Blame Technology Not Trade*", November 10, 2016

[5] **MRB *Theme Report***, "*The Brexit Dominos* ", July 7, 2016. Also, click *here* for a list of our Brexit related research reports.

[6] **MRB *Theme Report***, " *Investing Around Trumponomics* ", November 17, 2016. Also, click *here* for a list of our U.S. election related research reports.

Germany. Each of these have the potential to usher in protectionist policies.

Chart 3 MRB Assessment Of Foreign Exchange Markets




* MRB's assessment; includes weighted sum of relative growth (25%), policy/rate differentials (25%), trade/capital flows (20%), valuation (15%), and technicals (15%); range is -100 to 100
Note: Drivers of performance are for a 6-12 month horizon
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In an isolationist policy environment, the U.S. dollar should benefit, at least initially. This is not supportive for the U.S. economy, as household discretionary incomes would be squeezed by higher consumer prices (as higher priced domestic goods and services replace lower-priced imports) and borrowing costs. Also, corporate profits would suffer and the employment backdrop would deteriorate materially, even though the desire of such policies would be to create jobs for unskilled workers. That said, the U.S. economy and dollar would likely be the "best horse in the glue factory" as most other economies would suffer, creating deflationary pressures and downward pressure on their currencies. Although the initial flight-to-safety would benefit the U.S. dollar, this is not a bullish long-term story. Anti-trade and anti-immigration ends up protecting inefficiencies, undermines competitiveness and curtails potential growth. It would also encourage the world to seek out another reserve currency (potentially a basket of currencies). Still, investors are unlikely to look that far ahead for now.

Currencies of export-oriented economies would suffer the most, both from trade barriers and weaker global growth (which on its own softens import demand). Commodity currencies would be hardest hit. The extent to which the euro suffers would depend on whether the region is contributing to political instability (i.e. the outcome of the upcoming political events and the policies adopted will be critical). Conversely, the winner would be the Swiss franc, which is a traditional safe-haven and would benefit from external political instability. The Swiss economy is trade-oriented, but in good shape, competitive and its exports are not likely to be the focus of trade sanctions.

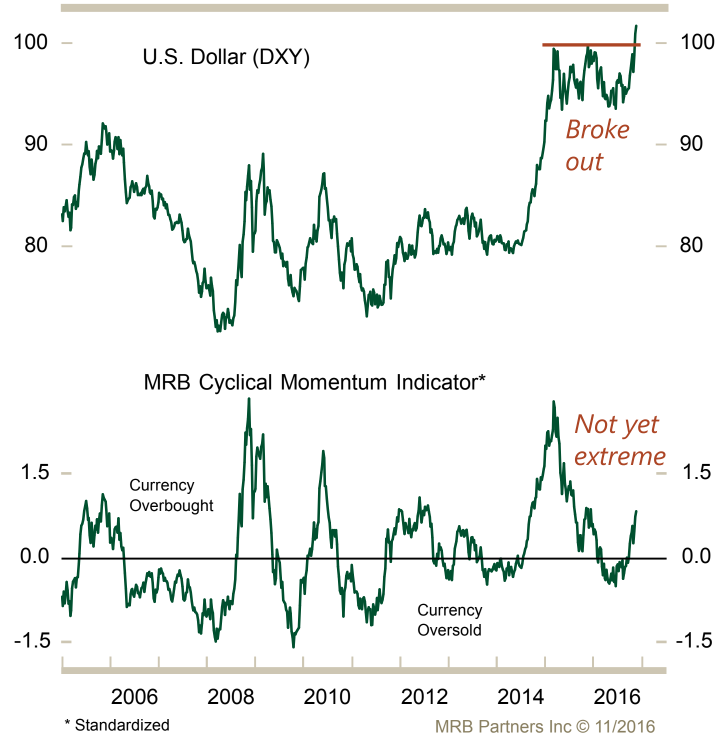
Everyone suffers from anti-trade policies

### *Netting Out These Forces*

We provide analysis and recommendations in the pages that follow for each of the major currencies, which accounts for these competing macro/policy forces and the current significant political uncertainty. As always, we also assess each market based on relative growth, interest rate differentials, trade/capital flows, valuation and technicals. **Chart 3** provides a snapshot aggregating these drivers for each of the currency markets. That said, our recommended investment strategy remains:

- Favor the U.S. dollar for now (**chart 4**). The dollar is pricey but has a favorable risk/reward profile since it should continue to be supported over the next few months in either macro backdrop. In a pro-growth environment, we expect the dollar to rise at a more gradual pace than as of late. If instead, the U.S. adopts isolationist policies the dollar could rise sharply. However, we would use this as an opportunity to gradually sell and begin positioning for a structural short.

Chart 4 **U.S. Dollar: Broad-Based Strength**




- Be very selective in export-oriented currencies until there is greater clarity on global anti-trade policies. These currencies are cheap and offer an appealing opportunity if the push towards protectionism subsides and global growth improves. If not, they will remain exposed. Thus, within a global currency portfolio, we remain underweight for now. However, for those looking to nibble, we recommend being selective and focusing on non-commodity currencies, where the country has significant domestic growth drivers and/or a smaller export sector relative to GDP.

- Hold the Swiss franc within a global currency portfolio as an insurance policy against political instability. In a pro-growth backdrop, we expect the Swiss franc to underperform the U.S. dollar. However, downside will be gradual and the currency provides a hedge against disruptive U.S. and/or European policies. Thus, we maintain a neutral allocation on the franc versus the dollar.

- Underweight the euro until regional political clouds clear. There is a decent chance that euro area politics will follow the path of the U.K. and U.S., which would again undermine confidence in the monetary union and currency. Thus, investors should limit exposure for now, by maintaining a mild underweight versus the U.S. dollar. However, if politics do not shift in an isolationist direction, a global rotation towards euro area assets will likely occur sometime next year. The primary beneficiary will likely be regional equities, but the currency will find some support. For those looking to make this bet, we would trade the euro versus the yen, rather than against the U.S. dollar.

USD is still a good risk/reward bet

- Finally, it is too soon to bottom fish the pound. The currency is now cheap and deeply oversold. However, Brexit could wreak havoc on the domestic economy, especially if the housing bubble start to deflate. Thus, upside for the currency is likely to be capped, unless politics change substantially.

**Phillip Colmar | Santiago Espinosa | Frank Petrocca | Luke Ohba**

# Australia: *Underweight*

The Australian Dollar (AUD) bounced modestly off its lows versus the U.S. dollar (USD) earlier this year, but has largely traded sideways for much of 2016. Looking ahead, we expect the currency to gradually weaken.

**Relative Growth:** Real GDP and overall economic sentiment has been firm, supported by accommodative monetary conditions and the recent rise in commodity prices. That said, business investment, employment and wage growth are all weak. In short, relative growth is about neutral, but less durable than the U.S. and should shift to a mild drag once China's macroprudential policy tightening cools its housing market and related demand for commodities.

**Policy/Rate Differentials:** The RBA left policy rates unchanged at 1.5% earlier this month. Policymakers noted that "*low interest rates have been supporting domestic demand and the lower exchange rate since 2013 has been helping the traded sector*". The central bank concluded that policy should stay accommodative. In turn, interest rates differentials will continue to slowly narrow and weigh on the AUD, as the Fed resumes its tightening campaign.

**Trade/Capital Flows:** Australia's terms of trade have edged up along with commodity prices. However, the country runs persistent trade and current account deficits, and requires a cheap currency to bolster domestic competitiveness.

**Valuation:** Our *MRB Purchasing Power Partity (PPP) Measure* suggests that the AUD is around fair value. An undershoot is likely in the years ahead.

**Technicals:** The AUD is at neutral readings according to the MRB Cyclical Momentum Indicator, but speculators have built sizable net long positions. This leaves room for disappointment.

**Final Word:** *Stay underweight the AUD versus the USD.*

**Australia Foreign Exchange: Drivers Of Performance***

| | – | | N | | + |
|---|---|---|---|---|---|
| Relative Growth | | | ■ | | |
| Policy/Rate Differentials | | ■ | | | |
| Trade/Capital Flows | | ■ | | | |
| Valuation | | | ■ | | |
| Technicals | | | ■ | | |
| *Net Impact* | | ■ | | | |

* 6-12 month horizon; versus U.S. dollar
Note: + = positive, N = neutral, – = negative

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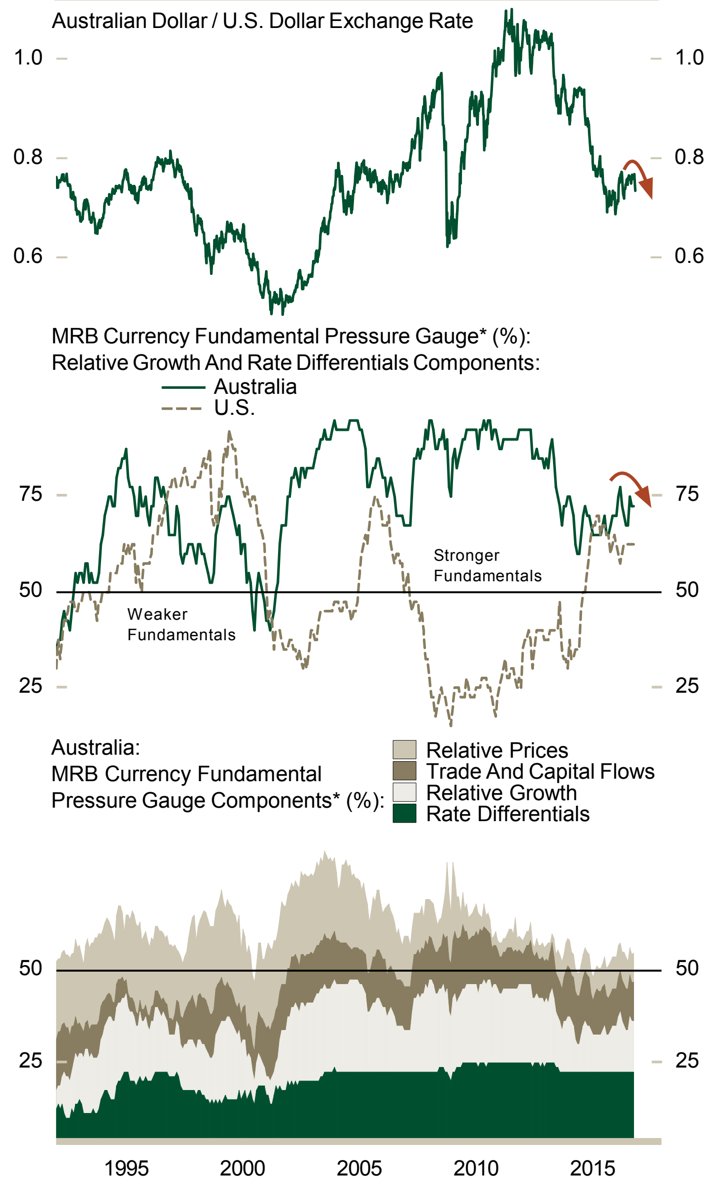
## Growth/Fundamentals




* Shown as a percentile ranking among developed markets

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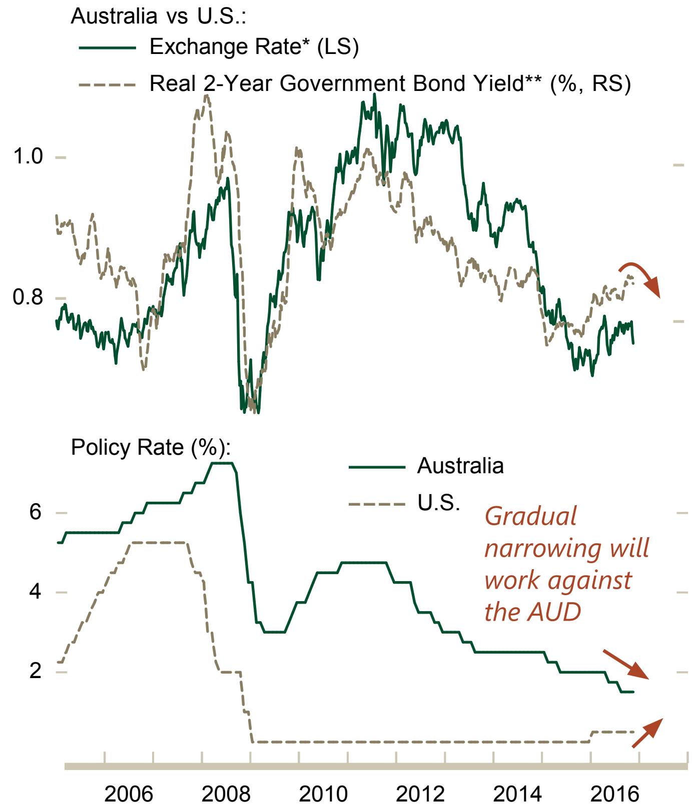
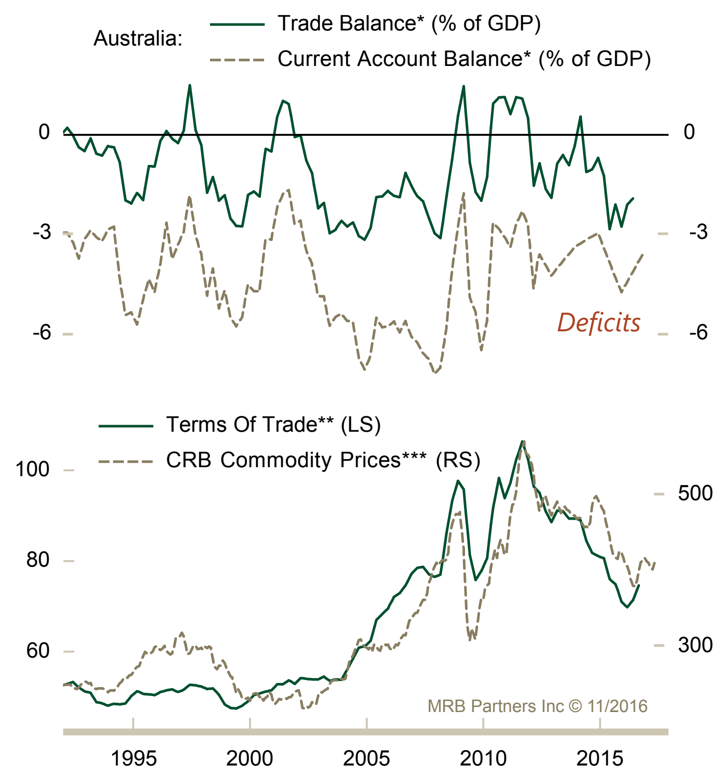
## Policy/Rate Differentials



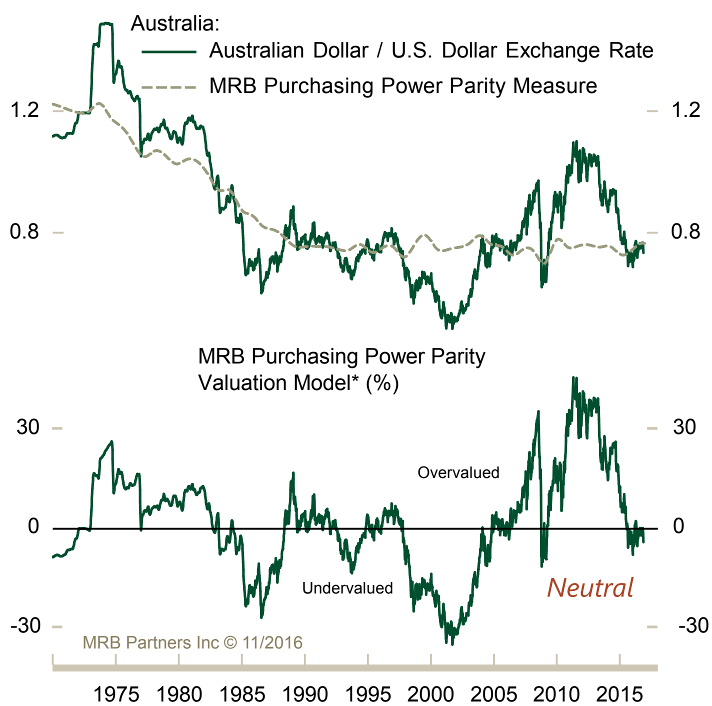

* Australian dollar / U.S. dollar exchange rate
** Deflated by headline CPI; Australia minus U.S. MRB Partners Inc © 11/2016

## Trade/Capital Flows



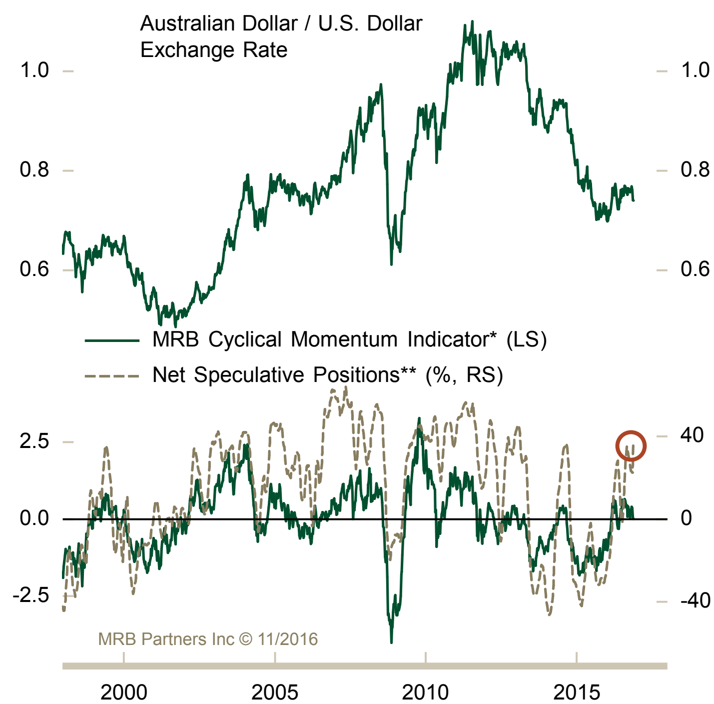

* Source: OECD
** Source: Australian Bureau of Statistics
*** Advanced 6 months; source: Commodity Research Bureau

## Valuation




* Percent deviation of currency from MRB Purchasing Power Parity Measure

## Technicals




* Standardized
** Total long positions minus total short positions divided by open interest; smoothed; source: Chicago Mercantile Exchange

# Canada: *Underweight*

The rise in energy prices earlier this year gave a lift to the Canadian dollar (CAD) versus the USD. Still, the currency was unable to punch through CAD/USD 0.80 and has since traded soft. Looking ahead, we are not bullish on crude oil prices or Canada's domestic fundamentals, and expect the petrocurrency to weaken.

**Relative Growth:** Domestic growth trends will remain a drag on the CAD. Housing excesses and a household credit binge have provided support for the economy in recent years, but these trends are exhausted. At the same time, business investment and employment growth have softened, and a weaker currency is needed to facilitate the multi-year rebalancing of the domestic economy.

**Policy/Rate Differentials:** The BoC left policy rates unchanged at 0.5% in mid-October and downgraded its growth outlook. Policymakers acknowledged that "*slower near-term housing resale activity and a lower trajectory for exports*" point to weaker domestic prospects. In short, interest rate differentials will slowly weigh on the currency as the Fed resumes tightening in December.

**Trade/Capital Flows:** Canada runs persistent trade and current account deficits. The currency will need to materially undershoot its longer-term equilibrium for an extended period to restore competitiveness and gradually encourage a rebuilding of the relatively small non-commodity export sector.

**Valuation:** The CAD is slightly undervalued according to the *MRB PPP Measure*, albeit the latter is starting to erode.

**Technicals:** The CAD is now mildly oversold based on most cyclical momentum measures, but not near readings that have historically signaled a durable bounce.

**Final Word:** *Stay underweight the CAD versus the USD.*

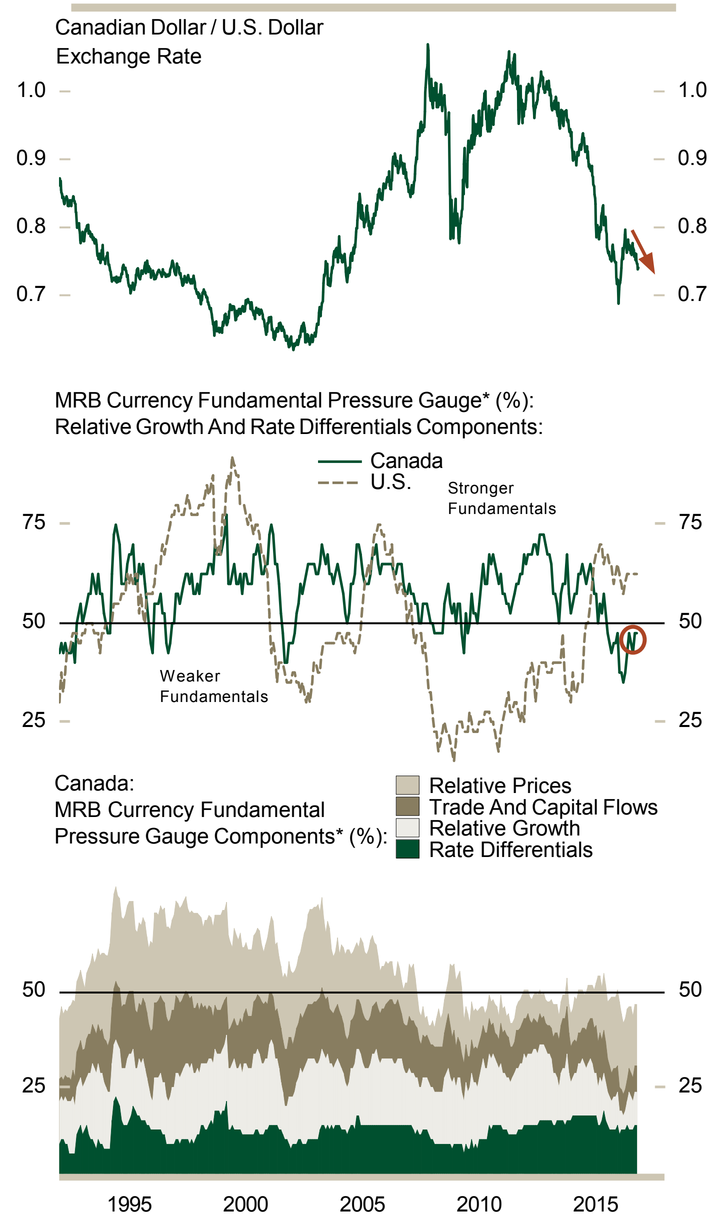
**Canada Foreign Exchange: Drivers Of Performance***

| | – | | N | | + |
|---|---|---|---|---|---|
| Relative Growth | | ■ | | | |
| Policy/Rate Differentials | | ■ | | | |
| Trade/Capital Flows | | ■ | | | |
| Valuation | | | | ■ | |
| Technicals | | | | ■ | |
| *Net Impact* | | ■ | | | |

* 6-12 month horizon; versus U.S. dollar
Note: + = positive, N = neutral, – = negative

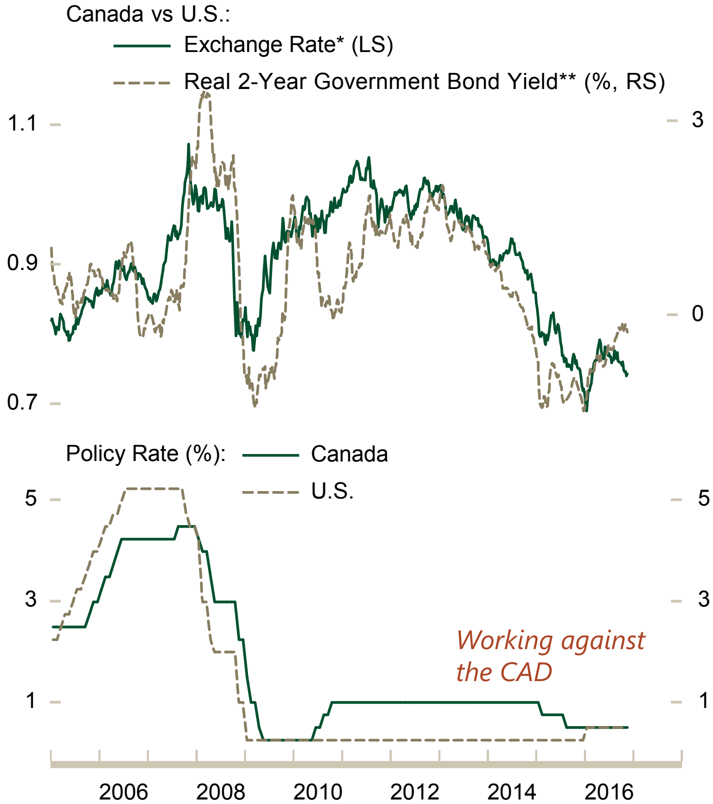


## Growth/Fundamentals



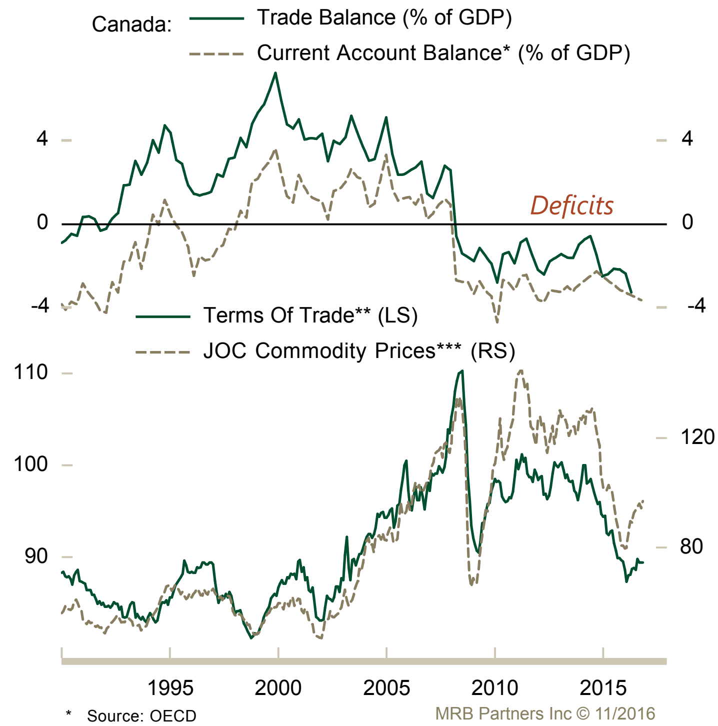

* Shown as a percentile ranking among developed markets

## Policy/Rate Differentials



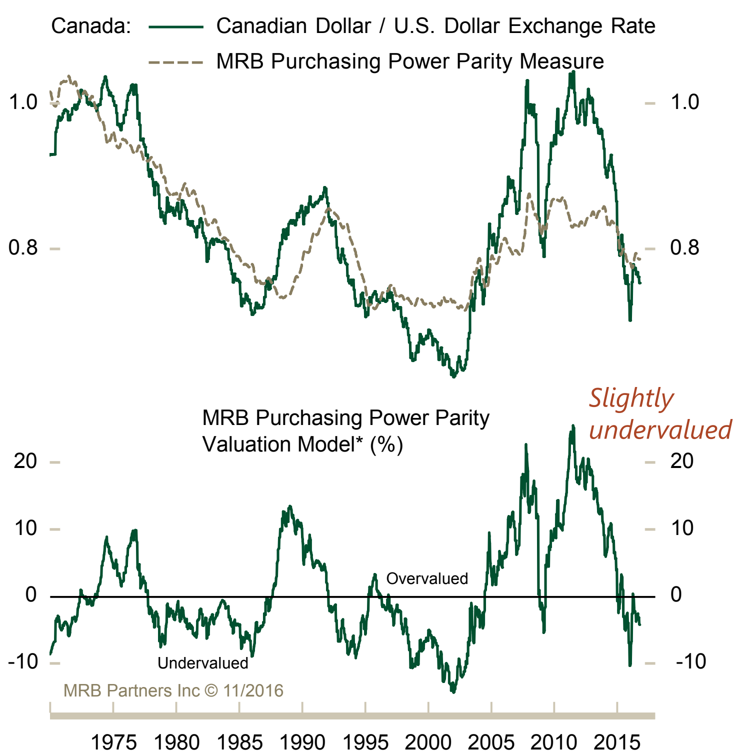

* Canadian dollar / U.S. dollar exchange rate
** Deflated by headline CPI; Canada minus U.S. MRB Partners Inc © 11/2016

## Trade/Capital Flows



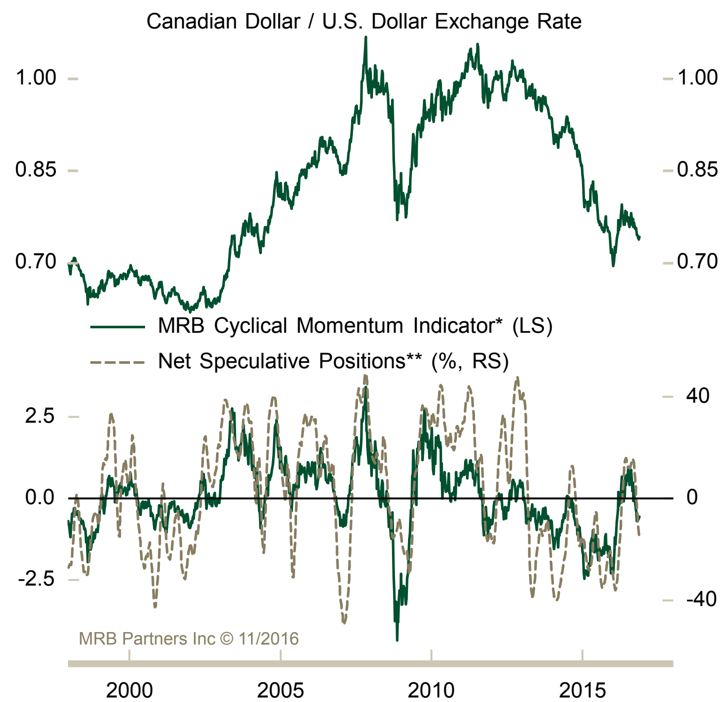

* Source: OECD
** Source: Thomson Reuters
*** Source: Journal of Commerce

## Valuation




* Percent deviation of currency from MRB Purchasing Power Parity Measure

## Technicals




* Standardized
** Total long positions minus total short positions divided by open interest; smoothed; source: Chicago Mercantile Exchange

# Euro Area: *Underweight*

The euro (EUR) has depreciated sharply against the USD recently, benefiting our underweight allocation. Although a near-term consolidation is probable, we continue to bet on some further weakness over the next 6-12 months.

**Relative Growth:** The growth differential between the euro area and U.S. has been minimal over the past year. The euro area economy continues along its modest growth path and underlying trends remain positive. That said, the U.S. economy is gaining momentum and could be fueled further by fiscal stimulus policies. Thus, relative growth could shift to a modest drag next year for the euro.

**Policy/Rate Differential:** The increased likelihood of a Fed rate hike next month has shifted interest rate differentials against the EUR. In contrast to the Fed, the ECB is likely to maintain its current stimulus measures at its December meeting, which will weigh on the EUR. Also, there are several upcoming regional elections with politicians running on anti-EMU mandates. These represent threats for the currency.

**Trade/Capital Flows:** The euro area's large current account and trade surpluses will provide some underlying support for the currency.

**Valuation:** The EUR is trading at roughly fair value based on the *MRB PPP Measure.*

**Technicals:** The EUR is now testing the low end of its multi-year trading range and will be vulnerable if it breaches these levels. That said, the currency is becoming oversold based on cyclical momentum measures and speculators are already heavily net short. Thus, a near-term digestion phase is likely before further weakness.

**Final Word:** *We remain underweight the EUR versus* the *USD, although favor the currency against many others including the yen and commodity currencies.*

**Euro Area Foreign Exchange: Drivers Of Performance***

| | - | | N | | + |
|---|---|---|---|---|---|
| Relative Growth | | | ■ | | |
| Policy/Rate Differentials | ■ | | | | |
| Trade/Capital Flows | | | | ■ | |
| Valuation | | | ■ | | |
| Technicals | | | | ■ | |
| *Net Impact* | | ■ | | | |

* 6-12 month horizon; versus U.S. dollar
Note: + = positive, N = neutral, - = negative
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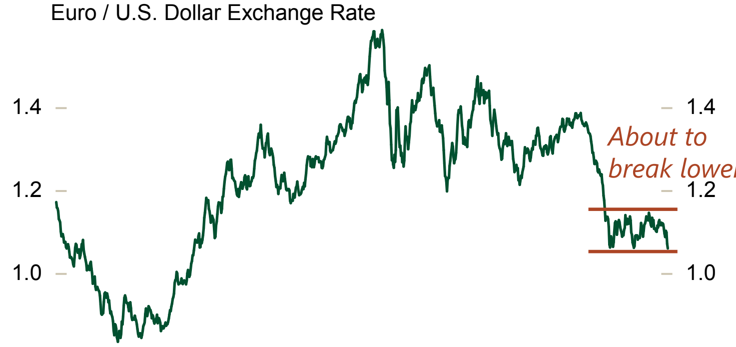
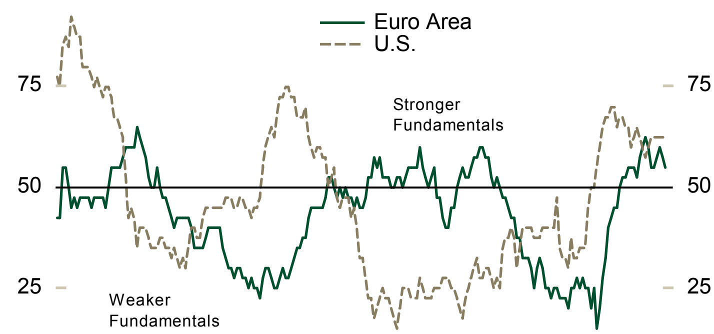
## Growth/Fundamentals

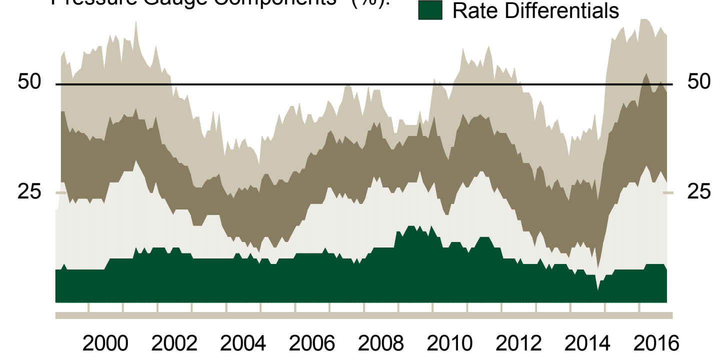
Euro / U.S. Dollar Exchange Rate




MRB Currency Fundamental Pressure Gauge* (%): Relative Growth And Rate Differentials Components:




Euro Area: MRB Currency Fundamental Pressure Gauge Components* (%):

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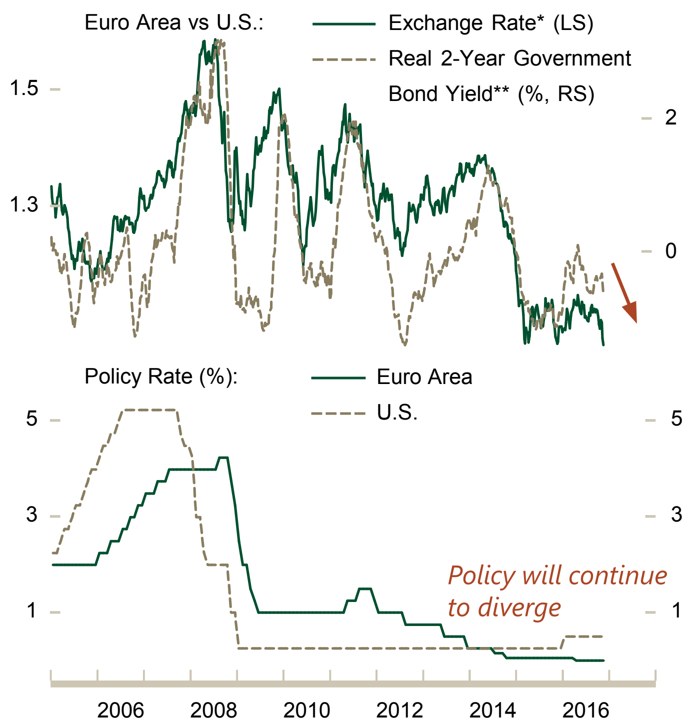
## Policy/Rate Differentials




* Euro / U.S. dollar exchange rate
** Deflated by headline CPI; Germany minus U.S.

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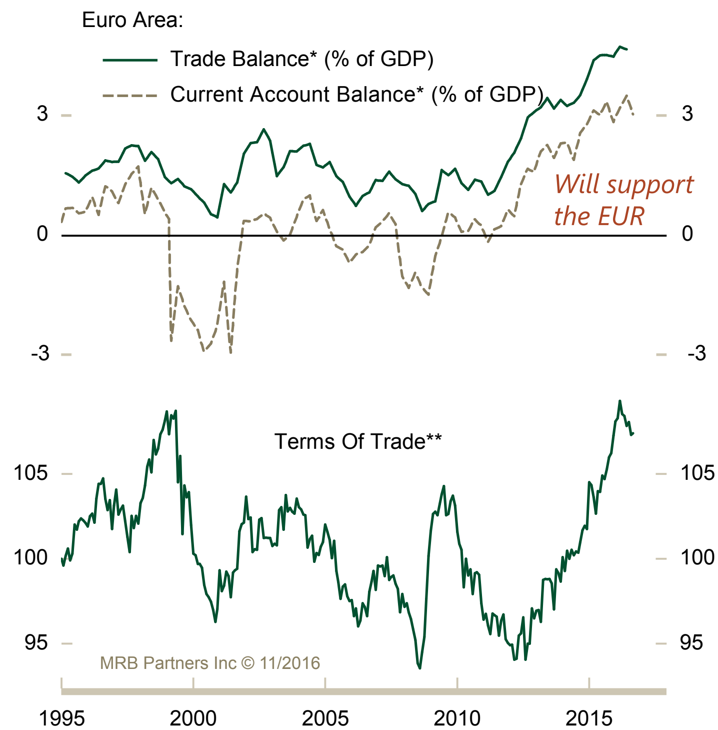
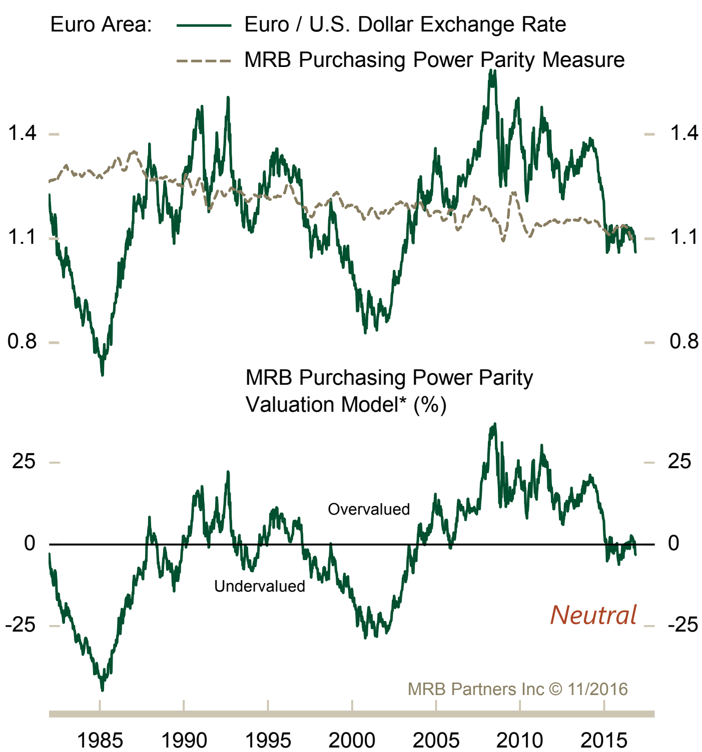
## Trade/Capital Flows



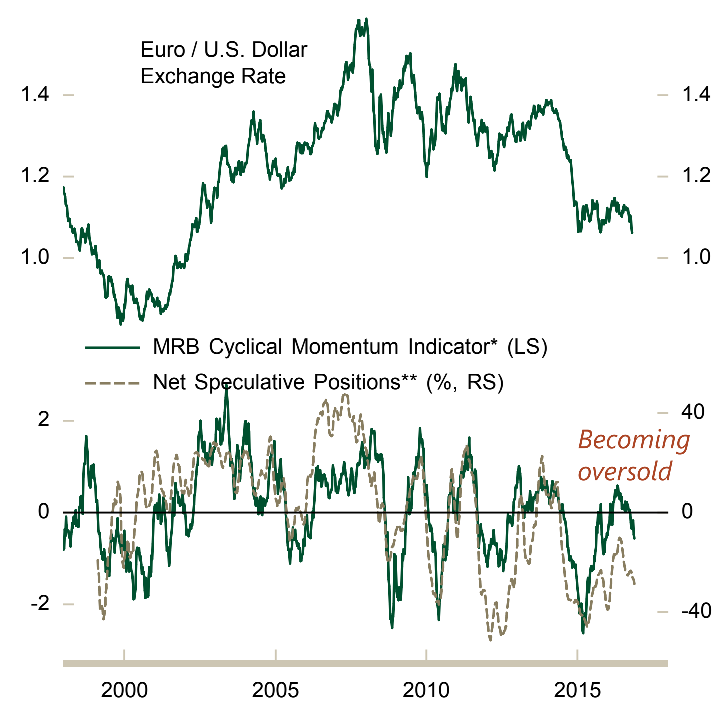

* Source: OECD
** Rebased; equally-weighted aggregate of France, Germany, Italy & Spain

## Valuation




* Percent deviation of currency from MRB Purchasing Power Parity Measure

## Technicals




* Standardized
** Total long positions minus total short positions divided by open interest; smoothed; source: Chicago Mercantile Exchange

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# Japan: *Underweight*

The yen (JPY) has depreciated materially against the USD on the back of deteriorating interest rate differentials and relatively weak domestic growth. We expect further downside.

**Relative Growth:** The Japanese economy has experienced a modest improvement in domestic growth, but conditions remain subdued. A weaker yen is needed in conjunction with fiscal and monetary support to encourage a more durable expansion. In short, relative growth will be a mild drag for the JPY.

**Policy/Rate Differentials:** The BoJ emphasized its reflationary commitment earlier this month, but is staying away from driving policy rates and yields further into negative territory. The BoJ introduced a policy in late September of "*yield curve control*" that will maintain 10-year JGB yields at roughly 0%. The BoJ will remain dovish for the foreseeable future, although interest rate differentials will now be influenced more by Fed policy.

**Trade/Capital Flows:** Weak commodity prices have boosted Japan's terms of trade and external accounts. However, a cheaper JPY is still required to bolster competitiveness.

**Valuations:** The JPY is undervalued based on the *MRB PPP Measure*, which should provide some underlying support for the currency.

**Technicals:** The recent sharp correction in the JPY has unwound cyclical overbought conditions and caused speculators to bail on their sizable net long positons. That said, momentum measures are only about neutral, leaving room for further downside before the JPY finds support.

**Final Word:** *Stay underweight the JPY versus the USD.*

**Japan Foreign Exchange: Drivers Of Performance***

| | – | | N | | + |
|---|---|---|---|---|---|
| Relative Growth | | ■ | | | |
| Policy/Rate Differentials | | ■ | | | |
| Trade/Capital Flows | | | ■ | | |
| Valuation | | | | ■ | |
| Technicals | | | ■ | | |
| *Net Impact* | | ■ | | | |

* 6-12 month horizon; versus U.S. dollar
Note: + = positive, N = neutral, – = negative

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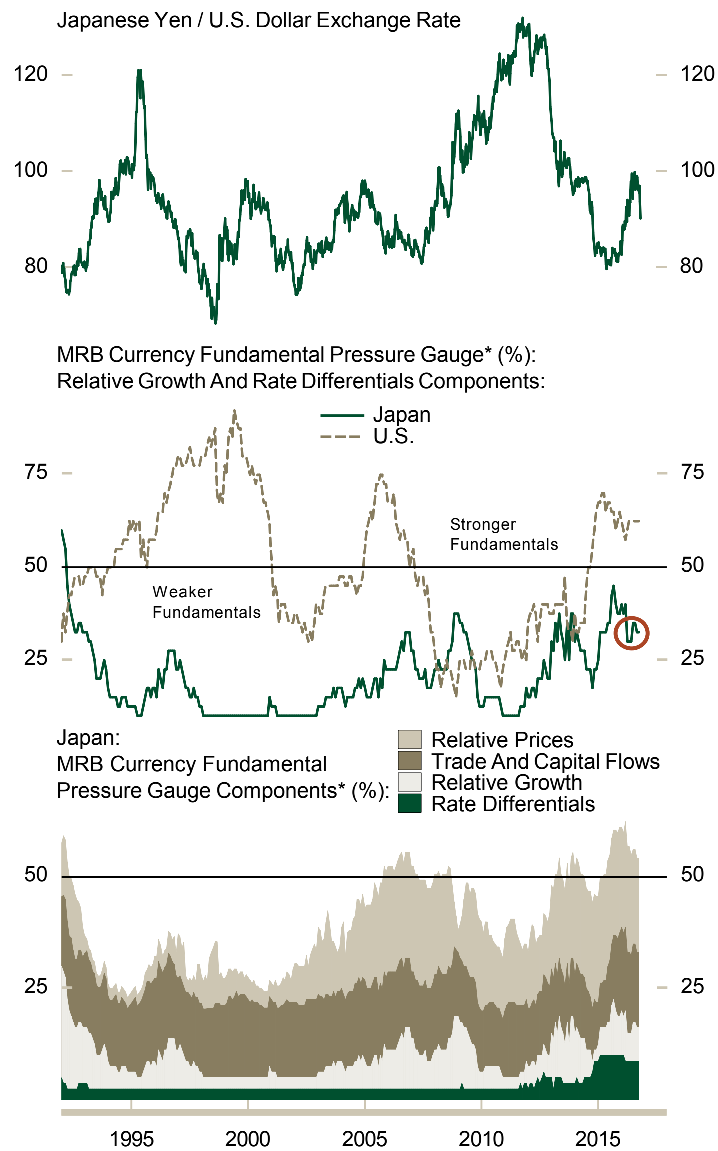
## Growth/Fundamentals




* Shown as a percentile ranking among developed markets

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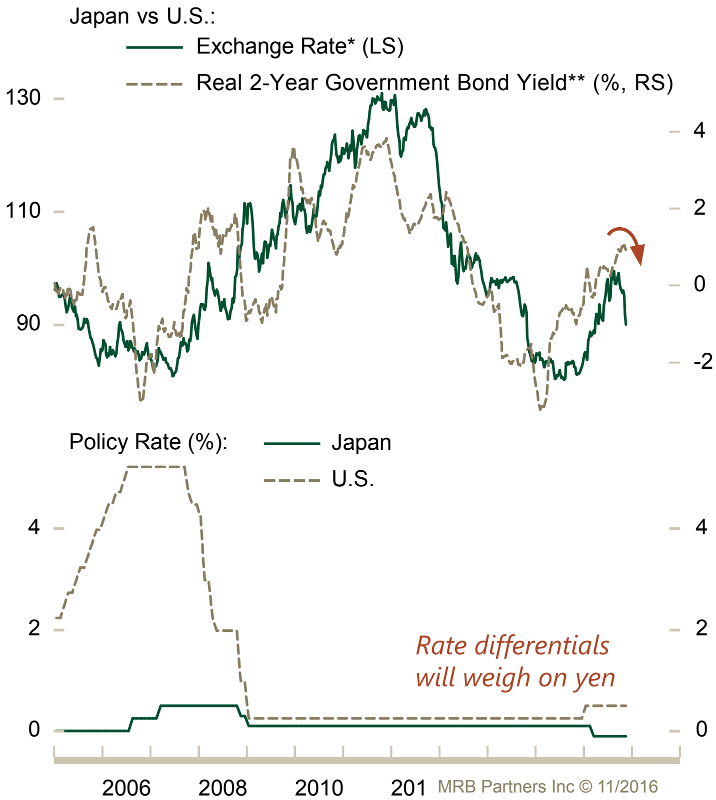
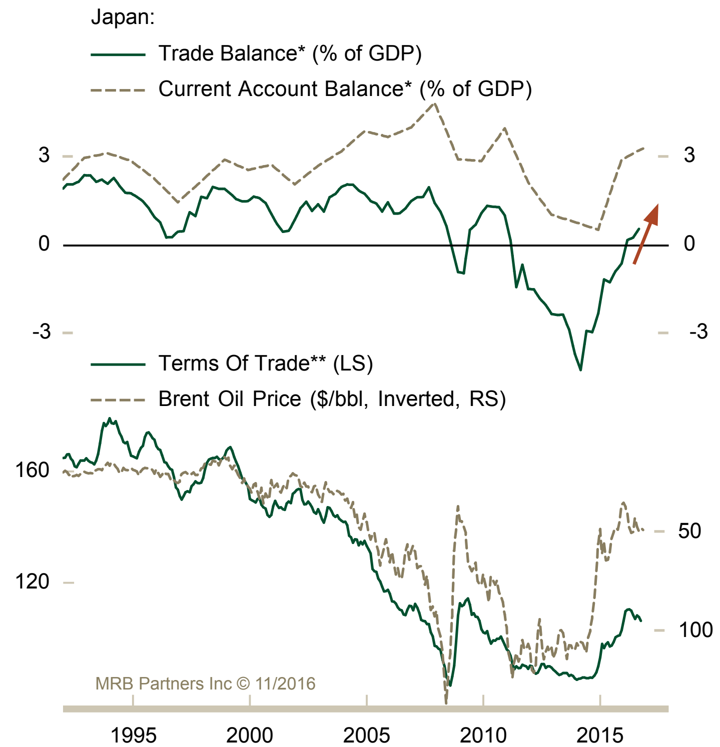
## Policy/Rate Differentials



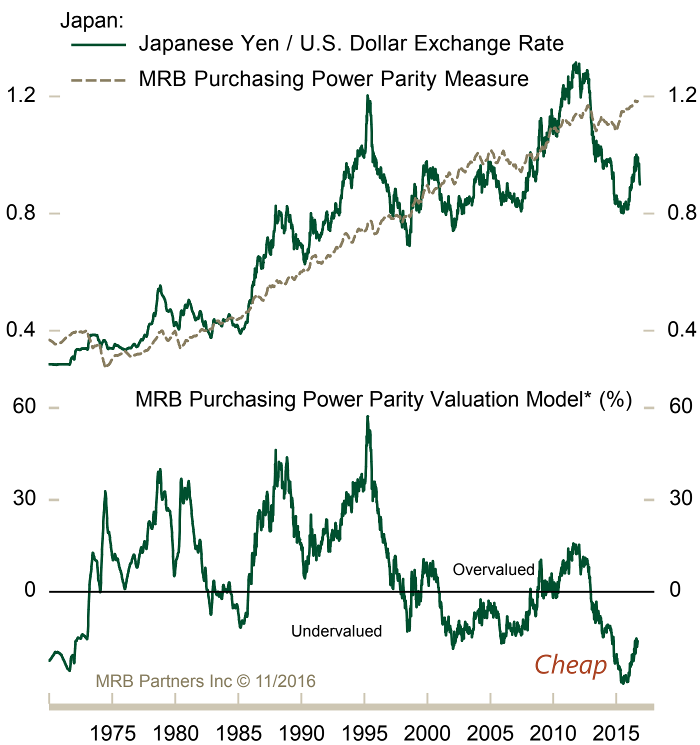

* Japanese yen / U.S. dollar exchange rate
** Deflated by headline CPI; Japan minus U.S.

## Trade/Capital Flows



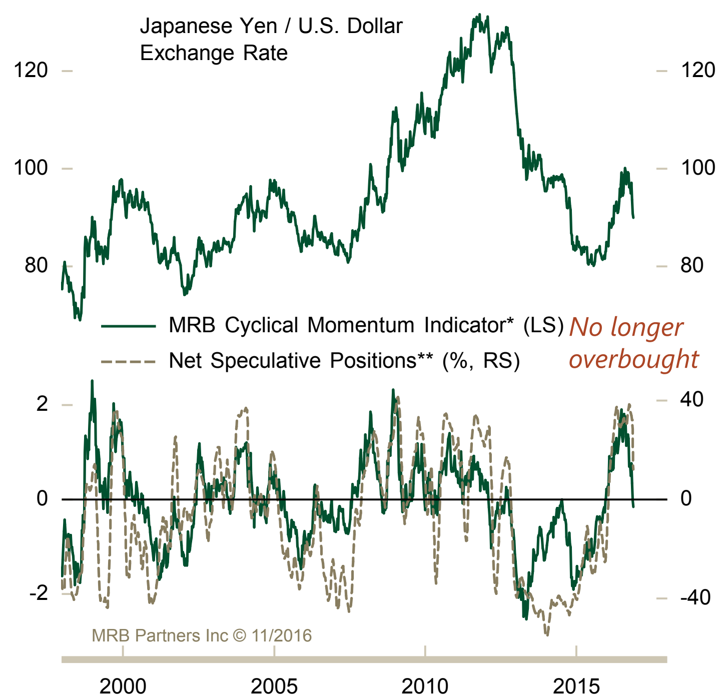

* Source: OECD
** Source: Bank of Japan

## Valuation




* Percent deviation of currency from MRB Purchasing Power Parity Measure

## Technicals




* Standardized
** Total long positions minus total short positions divided by open interest; smoothed; source: Chicago Mercantile Exchange

# New Zealand: *Underweight*

After appreciating against the USD this year, the New Zealand dollar (NZD) is starting to roll over. We expect weakness in the months ahead, mainly driven by narrowing interest rate differentials.

**Relative Growth:** Domestic growth conditions have been boosted by an accommodative monetary policy and stronger agricultural commodity prices. For now, relative growth conditions remain a support for the currency, but relative prospects could downshift as U.S. growth conditions strengthen.

**Policy/Rate Differentials:** The RBNZ cut rates this month by 25 bps to 1.75%. Policymakers expect the current policy stance to keep "*growth strong enough to have inflation settle near the middle of the target range*". However, the central bank notes that "*the exchange rate remains higher than is sustainable for balanced economic growth*" and that "a decline in the exchange rate is needed". Thus, either the currency weakens on its own, or interest rate differentials will continue to narrow.

**Trade/Capital Flows:** The modest recovery in commodity prices has provided support for New Zealand's terms of trade. However, New Zealand runs a persistent current account deficit and needs an undervalued exchange rate.

**Valuations:** The *MRB PPP Measure* suggest that the NZD is still overvalued.

**Technicals:** Most cyclical momentum measures for the NZD indicate that the currency is around neutral readings.

**Final Word:** *Stay underweight the NZD versus the USD.*

**New Zealand Foreign Exchange: Drivers Of Performance***

| | – | | N | | + |
|---|---|---|---|---|---|
| Relative Growth | | | | ■ | |
| Policy/Rate Differentials | | ■ | | | |
| Trade/Capital Flows | | ■ | | | |
| Valuation | | ■ | | | |
| Technicals | | | ■ | | |
| *Net Impact* | | ■ | | | |

* 6-12 month horizon; versus U.S. dollar
Note: + = positive, N = neutral, – = negative

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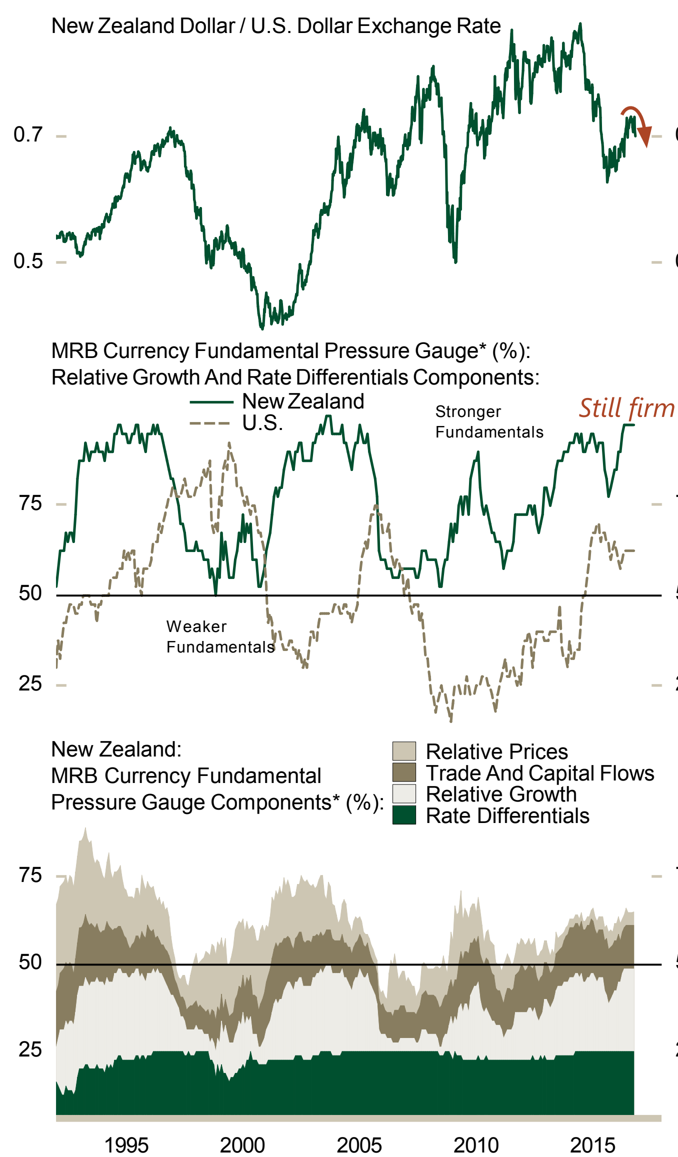
## Growth/Fundamentals




* Shown as a percentile ranking among developed markets

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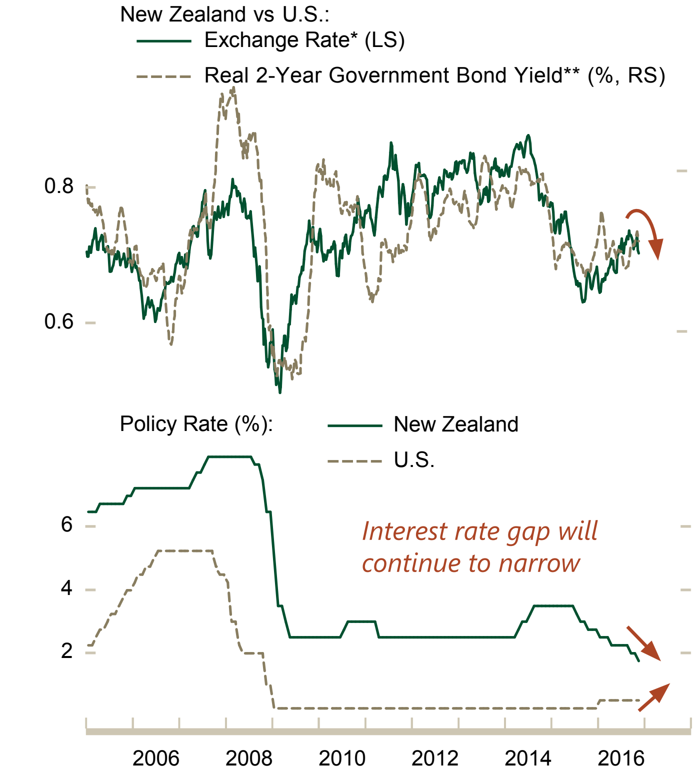
## Policy/Rate Differentials




* New Zealand dollar / U.S. dollar exchange rate
** Deflated by headline CPI; New Zealand (3-year) minus U.S.

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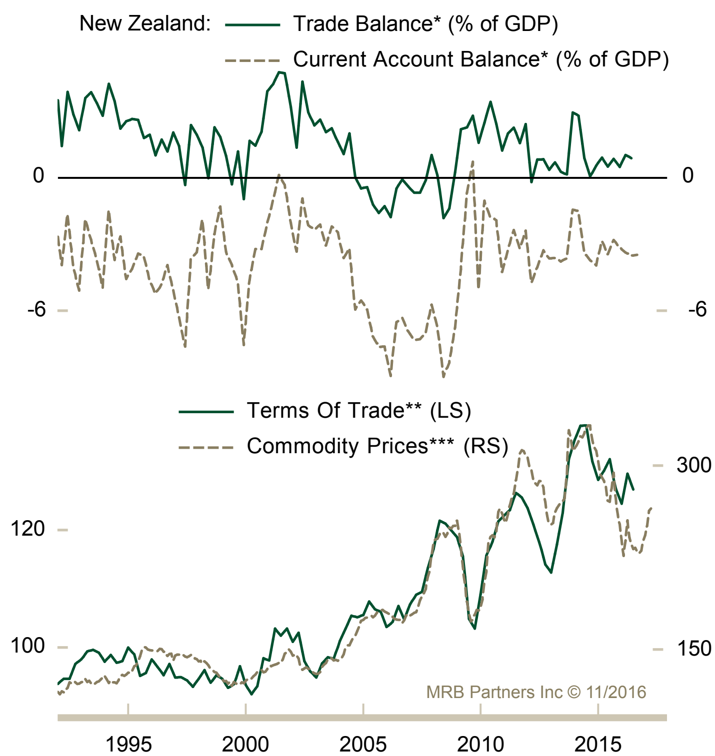
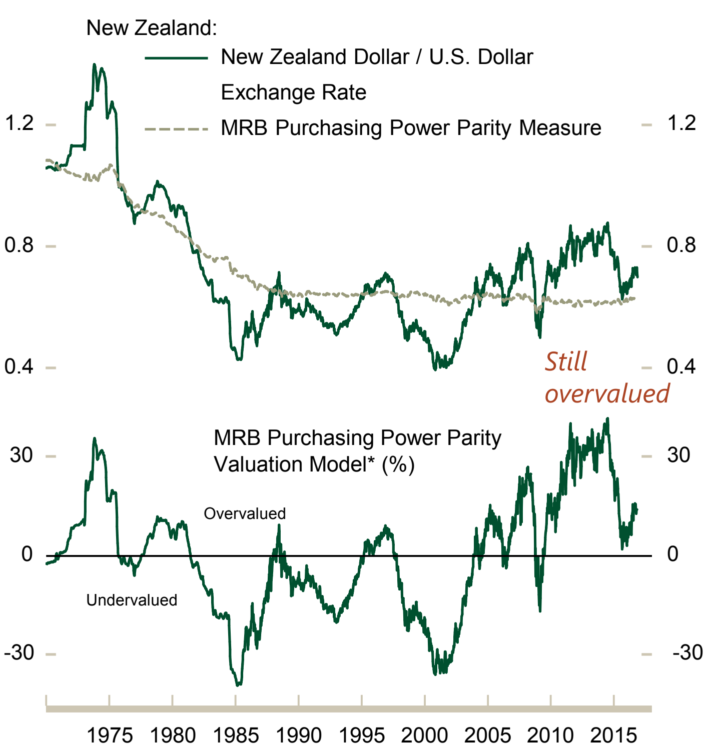
## Trade/Capital Flows




* Source: OECD
** Rebased to January 1995 = 100; source: Statistics New Zealand
*** Advanced 6 months; source: Australia and New Zealand Banking Group

## Valuation




* Percent deviation of currency from MRB Purchasing Power Parity Measure

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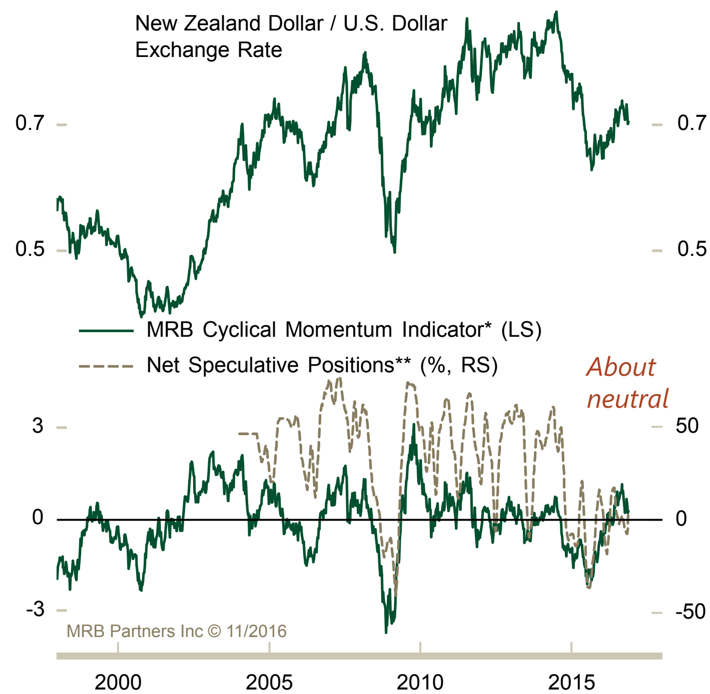
## Technicals




* Standardized
** Total long positions minus total short positions divided by open interest; smoothed; source: Chicago Mercantile Exchange

# Norway: *Underweight NOK/USD* *Underweight NOK/EUR*

The Norwegian Krone (NOK) has had difficulty lifting durably off its lows from early this year versus both the USD and EUR, despite the bounce in global energy prices. Underlying fundamentals remain poor and point to further weakness.

**Relative Growth:** Real economic growth has started to contract in Norway as the economy enters recession. Business investment and confidence remain depressed and the employment outlook has deteriorated. In short, relative growth will weigh on the NOK.

**Policy/Rate Differentials:** The Norges Bank left interest rates at 0.5% in late October, but maintained an easing bias for the year ahead. Interest rate differentials will remain a drag on the NOK.

**Trade/Capital Flows:** Norway's term of trade has bounced along with global energy prices, although this should fade. The country's trade surplus has evaporated over the past couple of years.

**Valuations:** The NOK is deeply undervalued based on the *MRB PPP Measure*, which should limit further downside. However, a weaker currency is needed as part of the reflationary strategy for the domestic economy.

**Technicals:** After several months of consolidating previous losses, the NOK is at neutral readings according to most cyclical momentum measures.

**Final Word:** *Stay underweight the NOK versus both the USD and the EUR.*

**Norway Foreign Exchange: Drivers Of Performance***

| | - | | N | | + |
|---|---|---|---|---|---|
| Relative Growth | ■ | □ | □ | □ | □ |
| Policy/Rate Differentials | □ | ■ | □ | □ | □ |
| Trade/Capital Flows | □ | ■ | □ | □ | □ |
| Valuation | □ | □ | □ | □ | ■ |
| Technicals | □ | □ | ■ | □ | □ |
| *Net Impact* | □ | ■ | □ | □ | □ |

* 6-12 month horizon; versus U.S. dollar
Note: + = positive, N = neutral, - = negative
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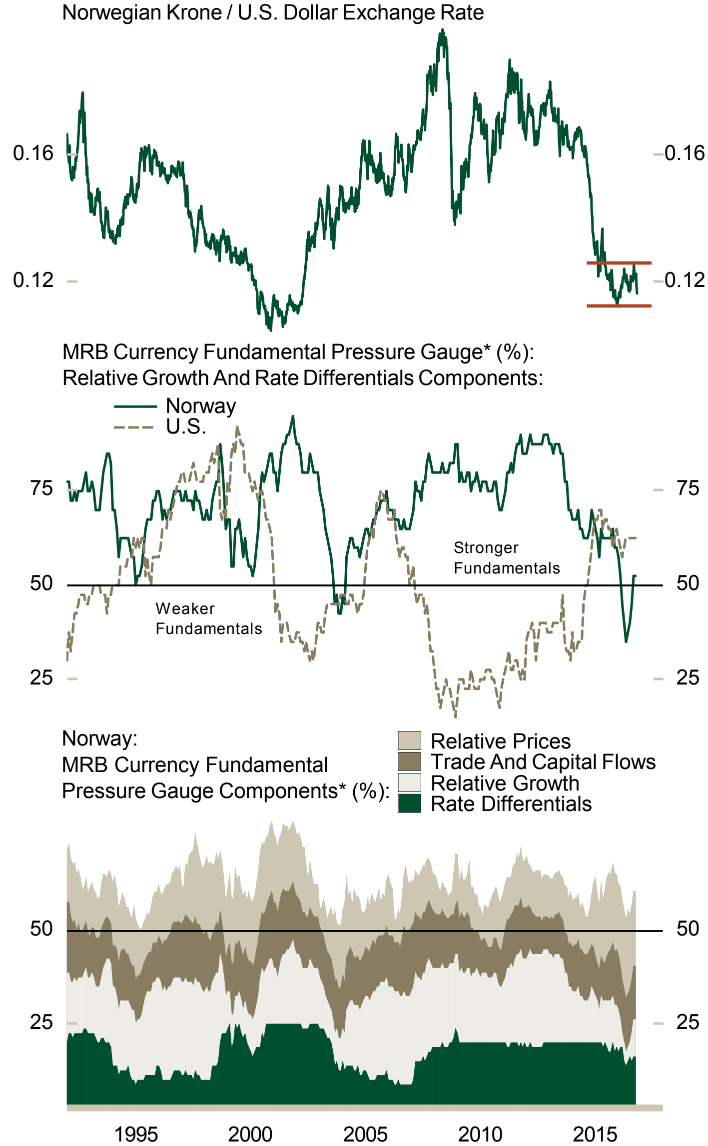
## Growth/Fundamentals




* Shown as a percentile ranking among developed markets
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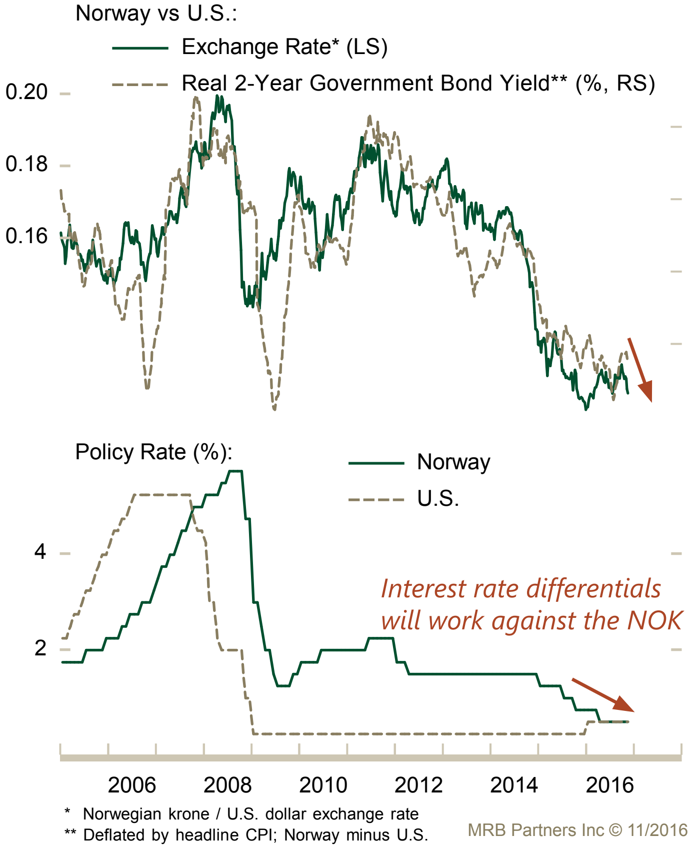
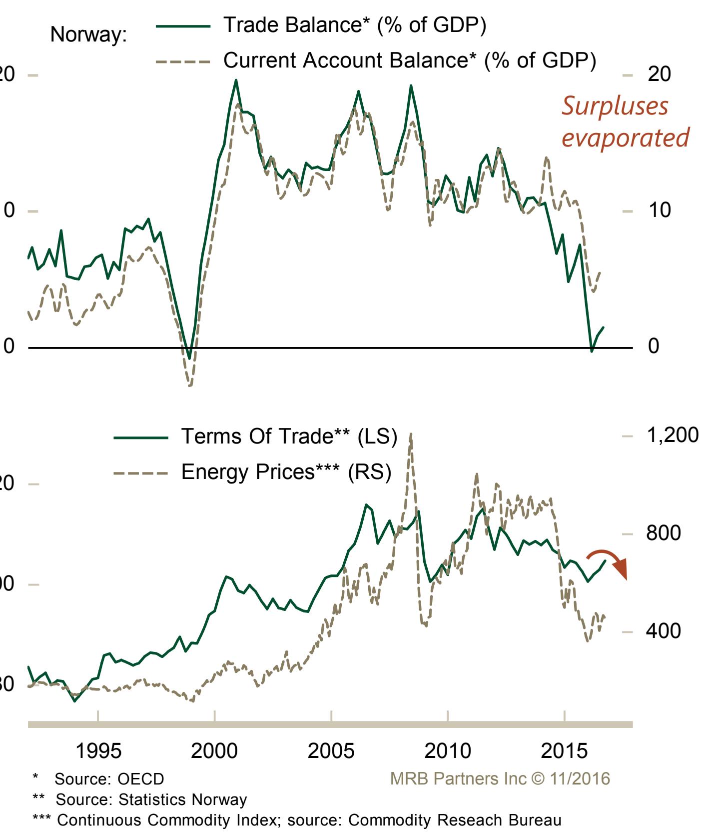
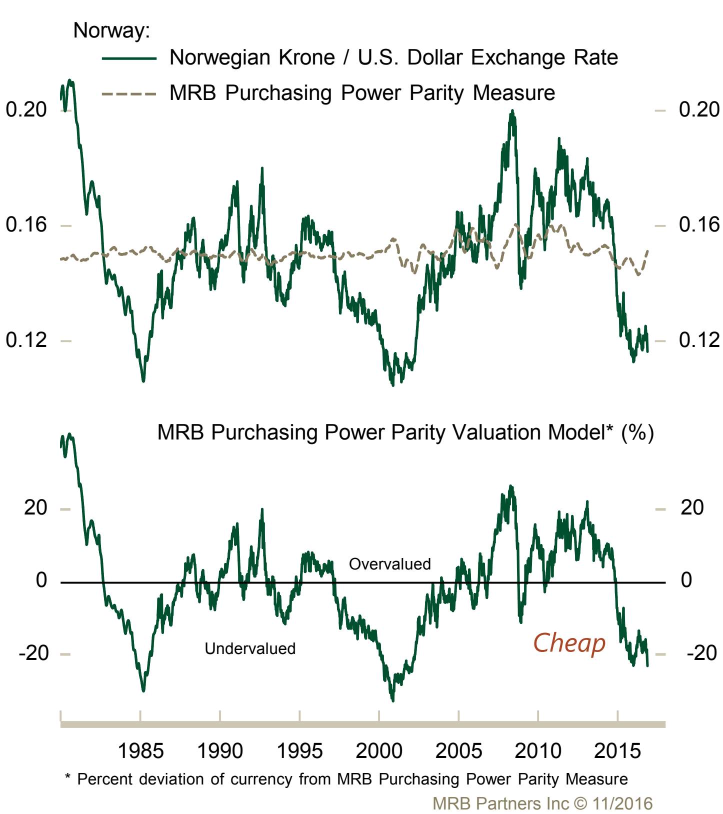
## Policy/Rate Differentials



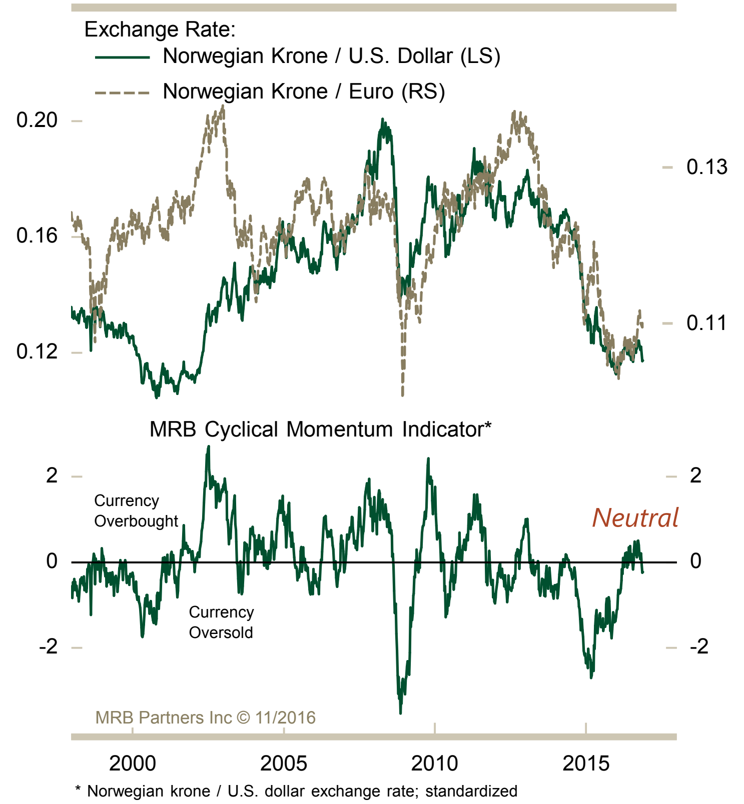

## Trade/Capital Flows




## Valuation




## Technicals



# Singapore: *Neutral SGD/USD Overweight SGD/EUR*

The Singapore Dollar (SGD) has depreciated sharply against the USD in line with the EUR. Global anti-trade policies (if implemented) are a threat for this currency. Thus, we continue to stand aside against the USD until there is greater clarity on U.S. (and European) policy.

**Relative Growth:** Economic activity in Singapore is sluggish in line with global export demand, albeit industrial production has picked up in recent months. Stronger global growth conditions bode well for trade and this export-oriented economy, provided protectionist policies are not adopted. We recommend waiting for greater clarity on this front from the U.S. before making a bet on the SGD.

**Policy/Rate Differential:** In mid-October the Monetary Authority of Singapore decided to maintain the trade-weighted currency's policy band at current levels. Given our other currency views, this policy stance may lead to some further near-term weakness against the USD and strength versus the EUR.

**Trade/Capital Flows:** Singapore runs large current account and trade surpluses, which will provide underlying support for the SGD.

**Valuation:** The SGD is undervalued based on the *MRB PPP Measure*, which should also provide some support.

**Technicals:** The *MRB Cyclical Momentum Indicator* shows the currency is now becoming oversold.

**Final Word:** *We remain neutral on the SGD versus the USD and overweight against the EUR. However, we acknowledge that the SGD will likely swing materially upon evidence of the extent to which U.S. (and European) anti-trade policies are adopted.*

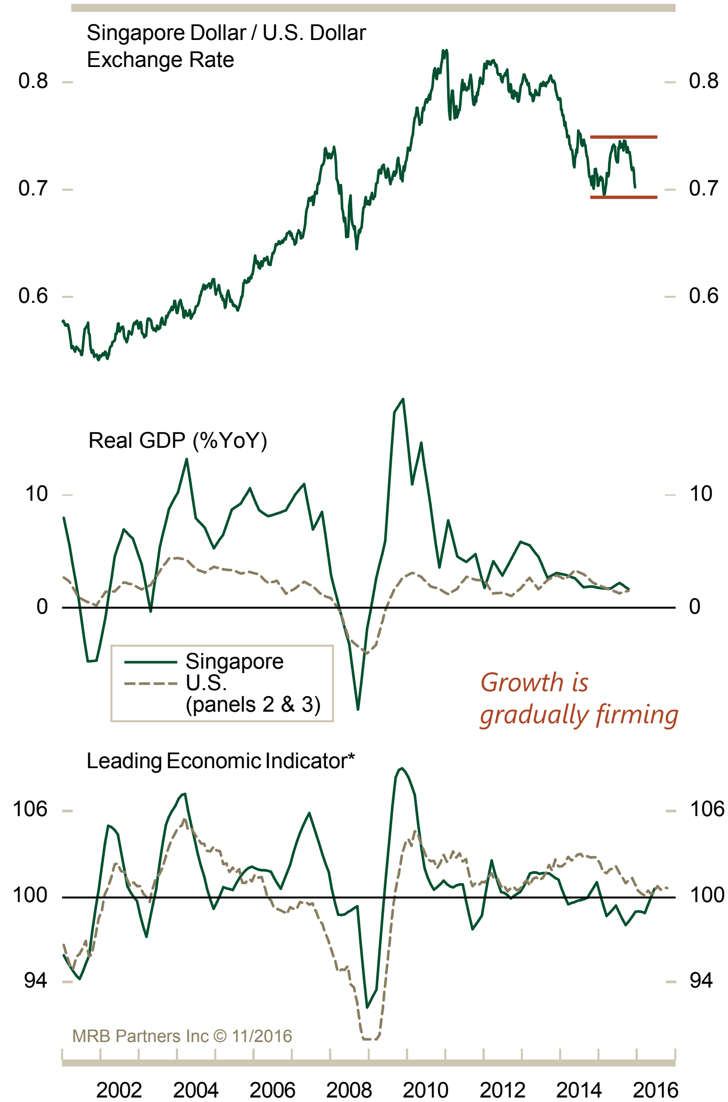
**Singapore Foreign Exchange: Drivers Of Performance***

| | - | | N | | + |
|---|---|---|---|---|---|
| Relative Growth | | | ■ | | |
| Policy/Rate Differentials | | ■ | | | |
| Trade/Capital Flows | | | | ■ | |
| Valuation | | | | ■ | |
| Technicals | | | | ■ | |
| *Net Impact* | | | ■ | | |

* 6-12 month horizon; versus U.S. dollar
Note: + = positive, N = neutral, - = negative

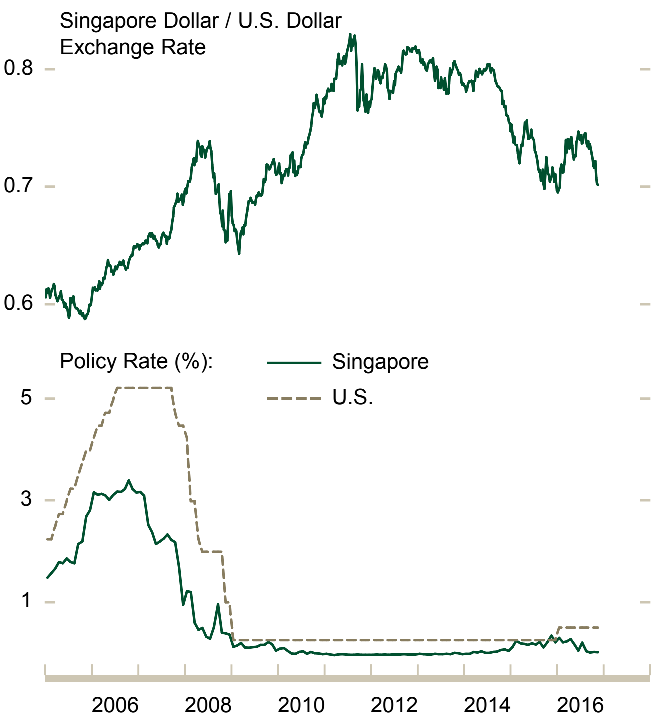


## Growth/Fundamentals

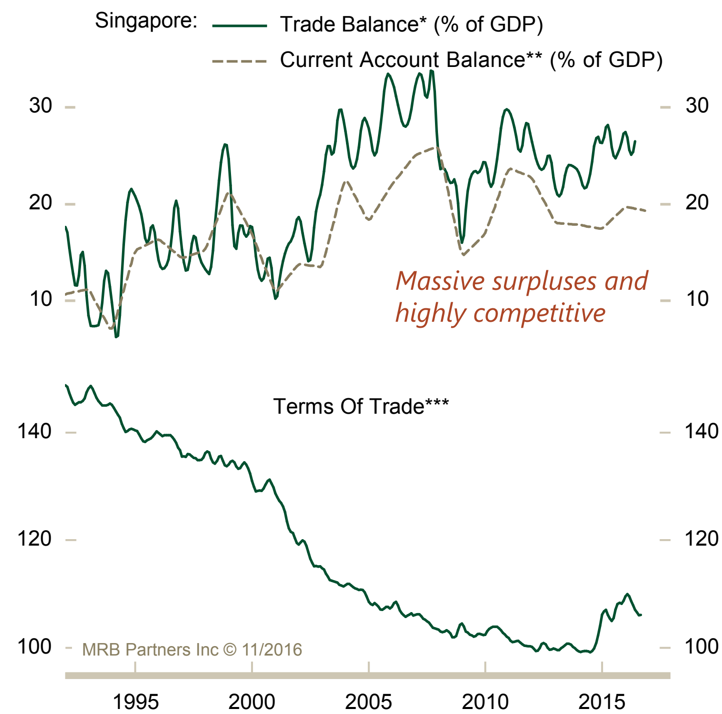



* Deviation from trend; U.S. truncated below 90; sources: Statistics Singapore and The Conference Board

## Policy/Rate Differentials

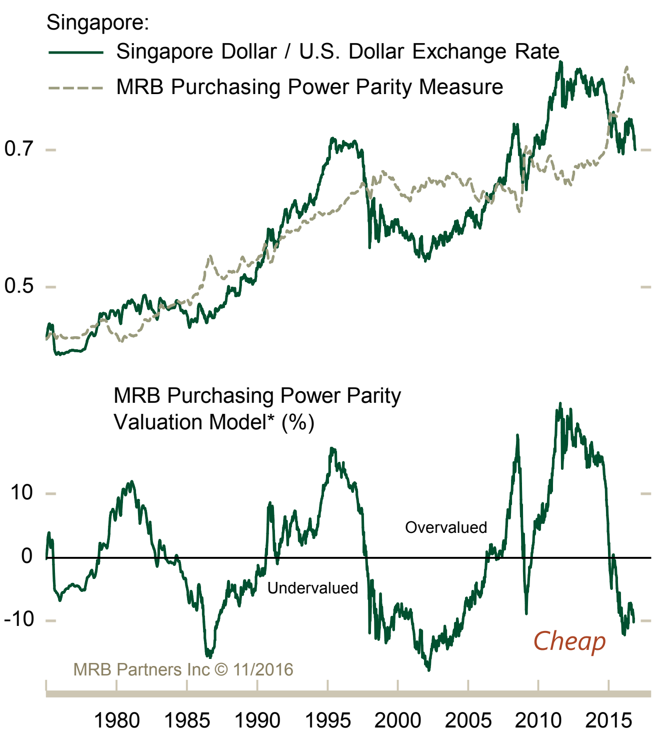



## Trade/Capital Flows



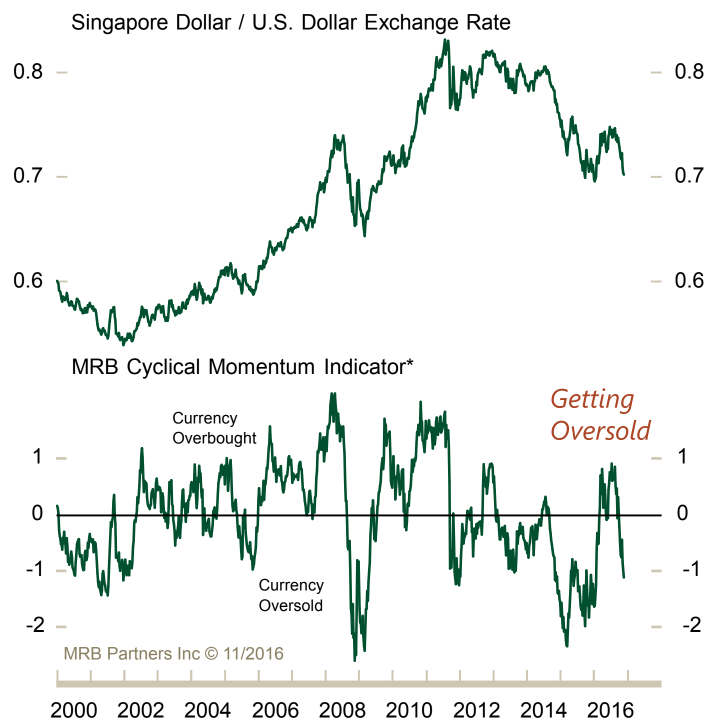

* Source: OECD
** Survey ranges from 1 to 9; 12-month moving average; source: IFO Institute
*** Smoothed; source: Statistics Singapore

## Valuation




* Percent deviation of currency from MRB Purchasing Power Parity Measure

## Technicals




* Standardized

# Sweden: *Neutral (Upgrade Bias) SEK/USD Overweight SEK/EUR*

The Swedish krona (SEK) broke the lower end of its multi-year trading range versus both the USD and EUR. Broad-based USD strength, continued extremely accommodative Riksbank policy, and global anti-trade rhetoric have put downward pressure on the currency. We like the SEK for domestic fundamental reasons, but acknowledge that calling a turning point has proved challenging.

**Relative Growth:** The aggressively easy monetary policy setting is fueling domestic growth in Sweden, as well as creating imbalances in the economy. House prices and household debt levels are becoming excessive, but relative growth still favors the SEK.

**Policy/Rate Differential:** The Riksbank reaffirmed its extremely dovish policy stance at its last meeting by hinting that it could extend the QE program into 2017. However, policymakers have since warned "*it is clear that we (the Riksbank) are approaching, maybe, a limit where we cannot buy (government bonds) much more*". Higher inflation and/or a pickup in global trade (provided anti-trade policies do not gain traction) will increase the pressure on the Riksbank to capitulate.

**Trade/Capital Flows:** Sweden has substantial trade and current account surpluses and the country is highly competitive. The economy will be able to withstand some SEK appreciation.

**Valuation:** The SEK is very undervalued according to the *MRB PPP Measure*.

**Technicals:** The recent selloff has left the SEK oversold based on the *MRB Cyclical Momentum Indicator*.

**Final Word:** *We are neutral on the SEK versus the USD, but look for an opportunity to add exposure if protectionism rhetoric subsides. We remain overweight the SEK versus the EUR.*

**Sweden Foreign Exchange: Drivers Of Performance***

| | - | | N | | + |
|---|---|---|---|---|---|
| Relative Growth | □ | □ | □ | ■ | □ |
| Policy/Rate Differentials | ■ | □ | □ | □ | □ |
| Trade/Capital Flows | □ | □ | □ | ■ | □ |
| Valuation | □ | □ | □ | □ | ■ |
| Technicals | □ | □ | □ | ■ | □ |
| *Net Impact* | □ | □ | □ | ■ | □ |

* 6-12 month horizon; versus U.S. dollar
Note: + = positive, N = neutral, - = negative

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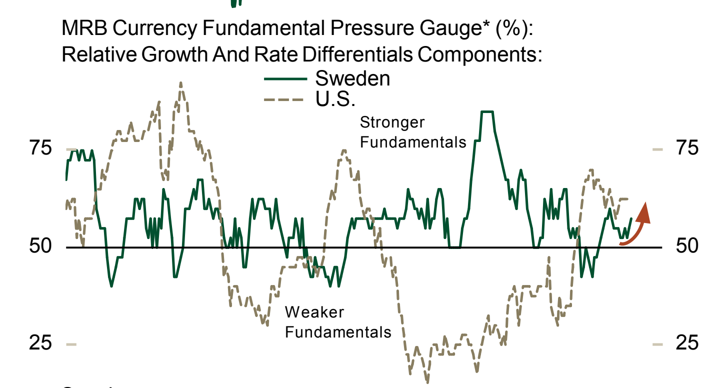
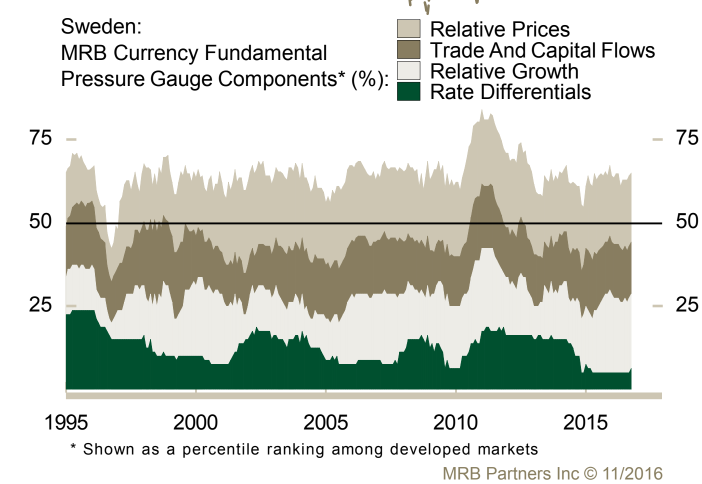
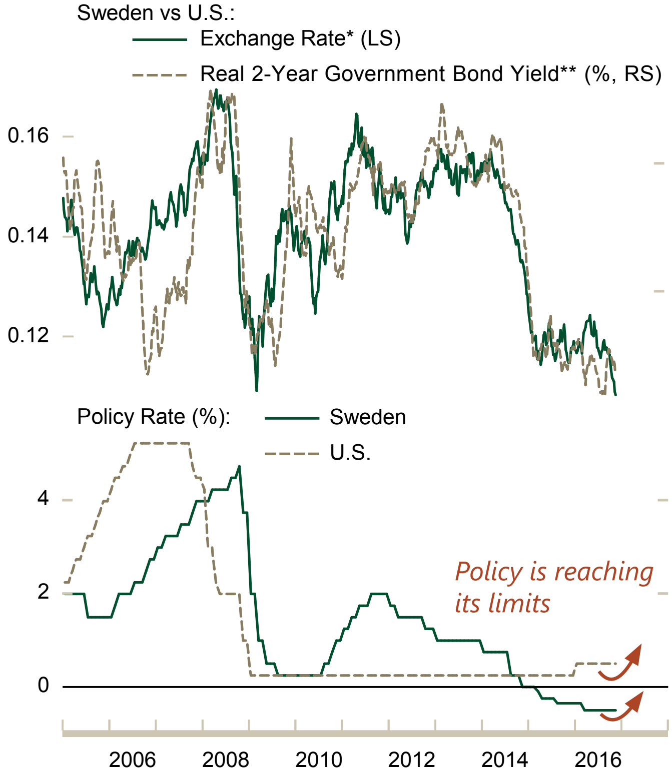
## Growth/Fundamentals

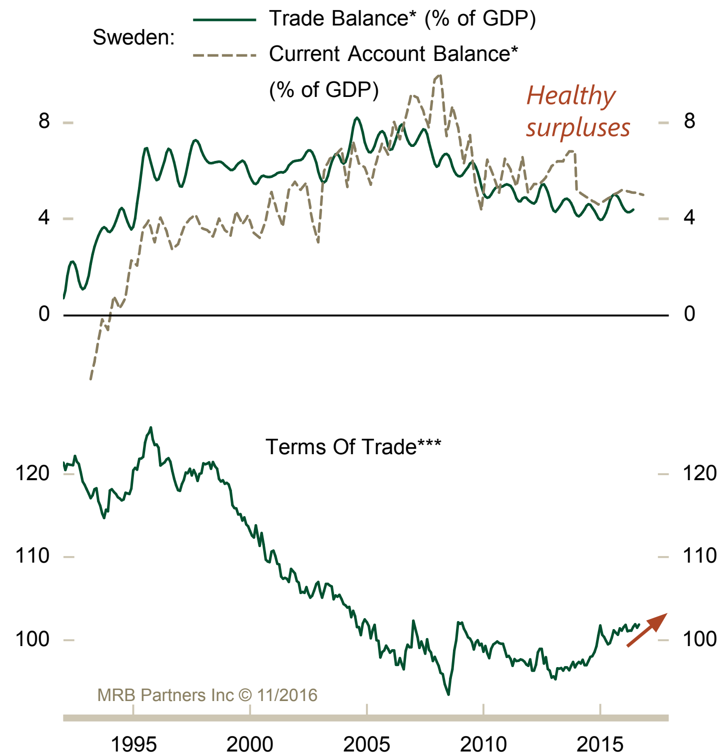



## Policy/Rate Differentials



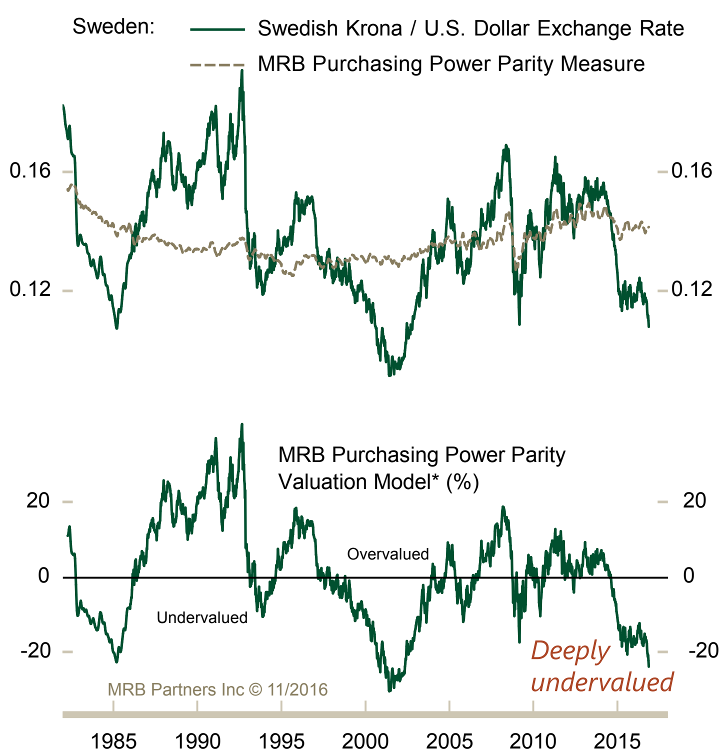

* Swedish krona / U.S. dollar exchange rate
** Deflated by headline CPI; Sweden minus U.S.

## Trade/Capital Flows



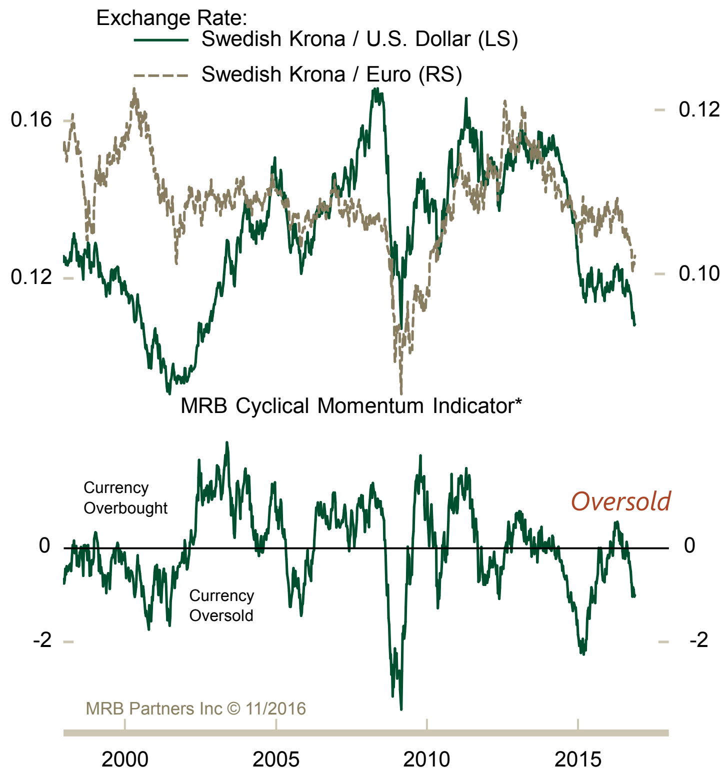

* Source: OECD
** Survey ranges from 1 to 9; 12-month moving average; source: IFO Institute
*** Source: Statistics Sweden

## Valuation




* Percent deviation of currency from MRB Purchasing Power Parity Measure

## Technicals




* Swedish krona / U.S. dollar exchange rate; standardized

# Switzerland: *Neutral CHF/USD Overweight CHF/EUR*

The Swiss franc (CHF) has moved lower versus the USD, while appreciating against the EUR. Although the CHF is likely to gradually weaken versus the USD, this traditional safe-haven provides insurance against political instability and warrants some exposure in a currency portfolio. For this reason, we are leaving our allocation at neutral versus the USD and overweight versus the EUR.

**Relative Growth:** The Swiss economy is slowly rebounding from cyclically depressed levels. The outlook is encouraging, with signs of improving trends in business confidence and the manufacturing PMI. Consequently, relative growth should be roughly neutral for the currency.

**Policy/Rate Differential:** The SNB will keep policy very accommodative for the foreseeable future and lag the Fed. Thus, interest rate differentials will be a headwind for the CHF versus the USD, while neutral against the EUR.

**Trade/Capital Flows:** Switzerland runs large trade and current account surpluses that provide underlying support for the currency.

**Valuation:** The CHF is deeply undervalued based on the *MRB PPP Measure.*

**Technicals:** Cyclical momentum measures are about neutral for the CHF versus the USD, but speculators are materially net short which should limit selling pressure.

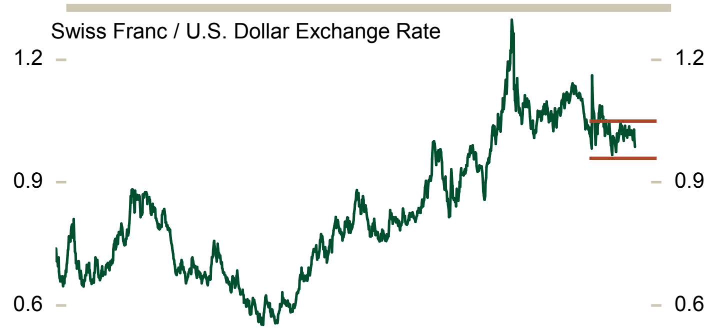
**Final Word:** *We remain neutral on the CHF versus the USD and overweight versus the EUR. The currency serves as a hedge against the possibility of greater political uncertainty emerging from the U.S. and Europe in 2017. Any evidence of anti-trade or anti-immigration policies that would be damaging for global growth will benefit the CHF.*

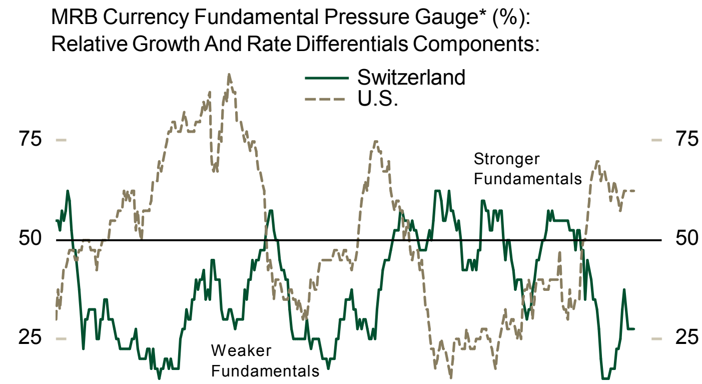
**Switzerland Foreign Exchange: Drivers Of Performance***

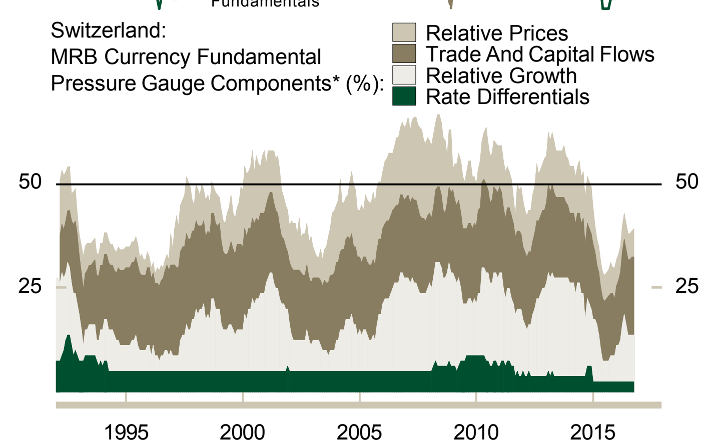
| | - | | N | | + |
|---|---|---|---|---|---|
| Relative Growth | | | ■ | | |
| Policy/Rate Differentials | | ■ | | | |
| Trade/Capital Flows | | | | ■ | |
| Valuation | | | | ■ | |
| Technicals | | | ■ | | |
| *Net Impact* | | | ■ | | |

* 6-12 month horizon; versus U.S. dollar MRB Partners Inc © 11/2016
Note: + = positive, N = neutral, - = negative

## Growth/Fundamentals




* Shown as a percentile ranking among developed markets
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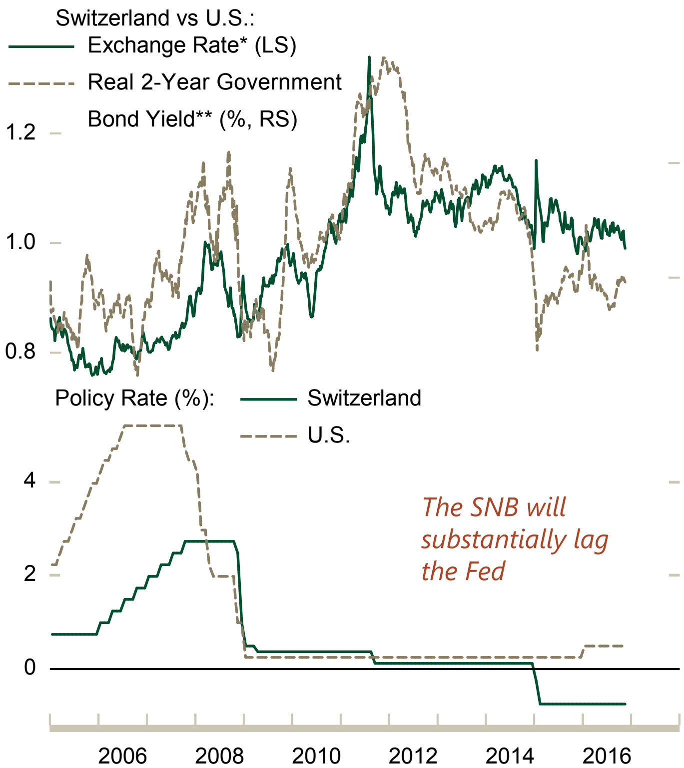
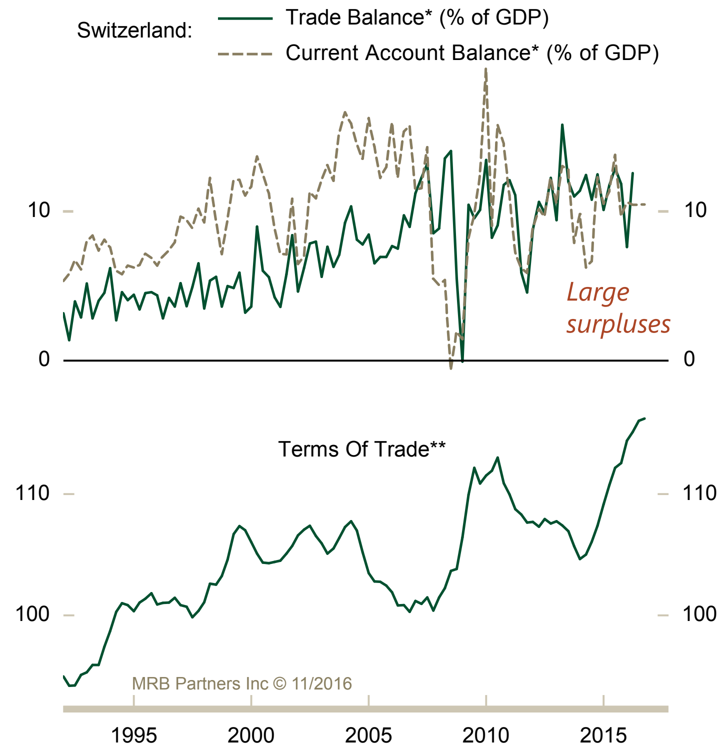
## Policy/Rate Differentials



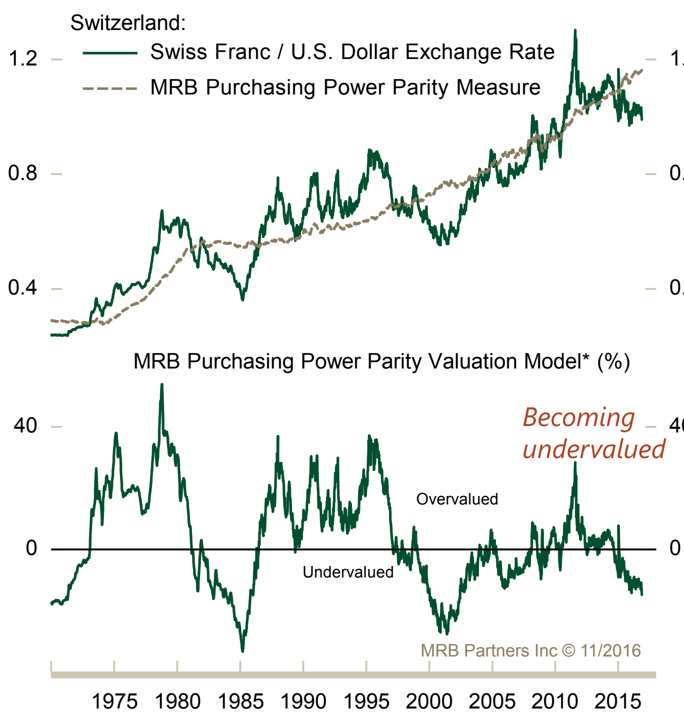

* Swiss franc / U.S. dollar exchange rate
** Deflated by headline CPI; Switzerland minus U.S.

## Trade/Capital Flows



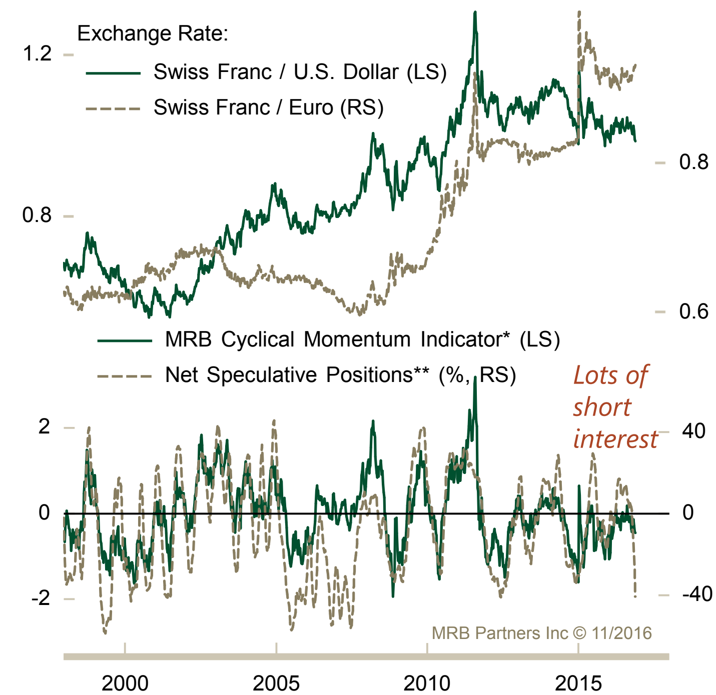

* Source: OECD
** Source: Swiss Economic Institute

## Valuation




* Percent deviation of currency from MRB Purchasing Power Parity Measure

## Technicals




* Swiss franc / U.S. dollar exchange rate; standardized
** Total long positions minus total short positions divided by open interest; smoothed; source: Chicago Mercantile Exchange

# U.K.: *Underweight GBP/USD* *Underweight GBP/EUR*

The pound (GBP) is showing tentative signs of stabilizing after renewed strong selling pressure when Prime Minister May suggested a hard Brexit scenario. Indeed, the pound has recouped some of its losses as Ms. May has struck a more business-friendly tone. That said, there is still room for some further depreciation as the economy weakens.

**Relative Growth:** Since the June referendum vote, the U.K. economy has held up better than expected, in part because the GBP melted and Article 50 has not yet been invoked. That said, business have largely canceled or shelved hiring and investment plans, which will act as a drag on relative growth and the GBP.

**Policy/Rate Differential:** The BoE will keep monetary policy highly accommodative. Governor Mark Carney stated that policymakers will tolerate "*some*" currency-induced overshoot of the inflation target to support the economy and employment (although so far the impact on CPI has been limited). On balance, interest rate differentials will be a weight on the GBP versus the USD.

**Trade/Capital Flows:** A weaker pound will be necessary to help improve competitiveness and reduce the large current account deficit.

**Valuation:** The GBP is now materially undervalued according to the *MRB PPP Measure*, which should help temper further downside.

**Technicals:** The GBP is now more than two standard deviations oversold based on the *MRB Cyclical Momentum Indicator* and speculators are heavily net short. Thus a further neart-term consolidation phase (or even countertrend bounce) is probable.

**Final Word:** *Stay underweight the GBP versus both the USD and EUR, but expect a digestion phase before further weakness.*

**U.K. Foreign Exchange: Drivers Of Performance***

| | – | | N | | + |
|---|---|---|---|---|---|
| Relative Growth | □ | ■ | □ | □ | □ |
| Policy/Rate Differentials | □ | ■ | □ | □ | □ |
| Trade/Capital Flows | □ | ■ | □ | □ | □ |
| Valuation | □ | □ | □ | □ | ■ |
| Technicals | □ | □ | □ | □ | ■ |
| *Net Impact* | □ | ■ | □ | □ | □ |

* 6-12 month horizon; versus U.S. dollar
Note: + = positive, N = neutral, – = negative

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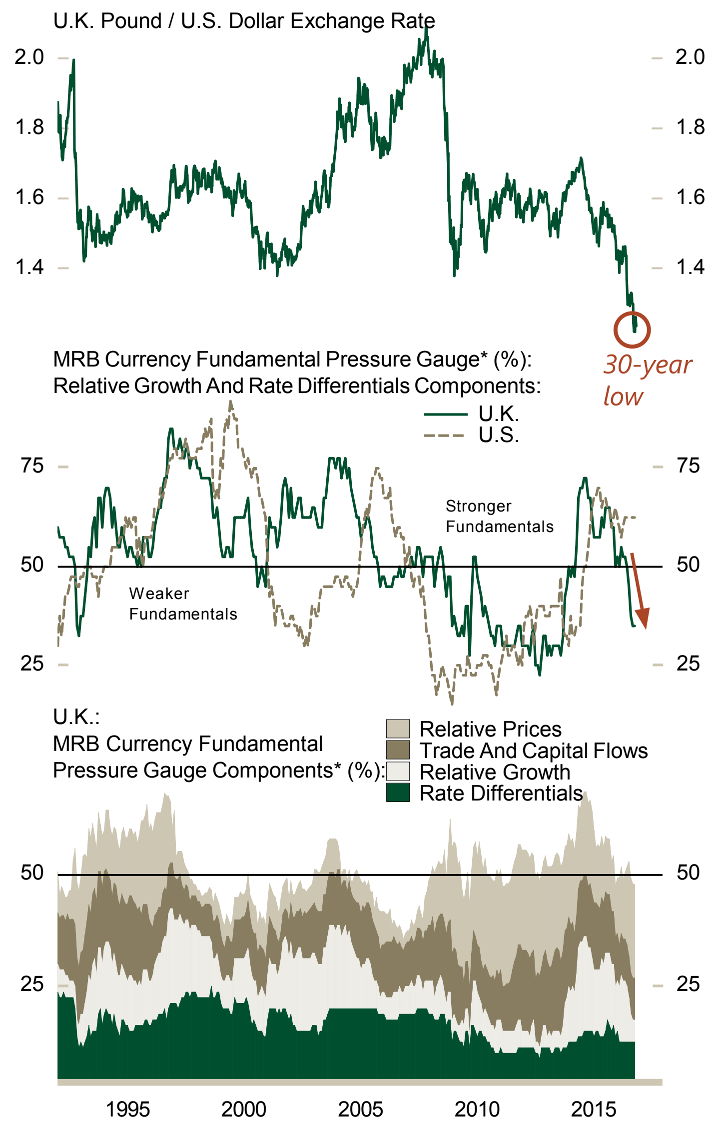
## Growth/Fundamentals




* Shown as a percentile ranking among developed markets

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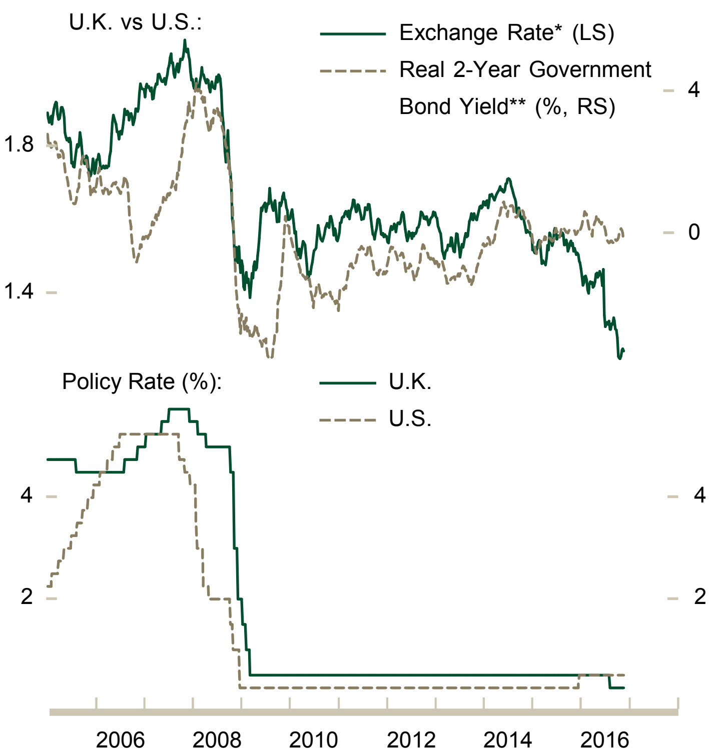
## Policy/Rate Differentials




* U.K. pound / U.S. dollar exchange rate
** Deflated by headline CPI; U.K. minus U.S.

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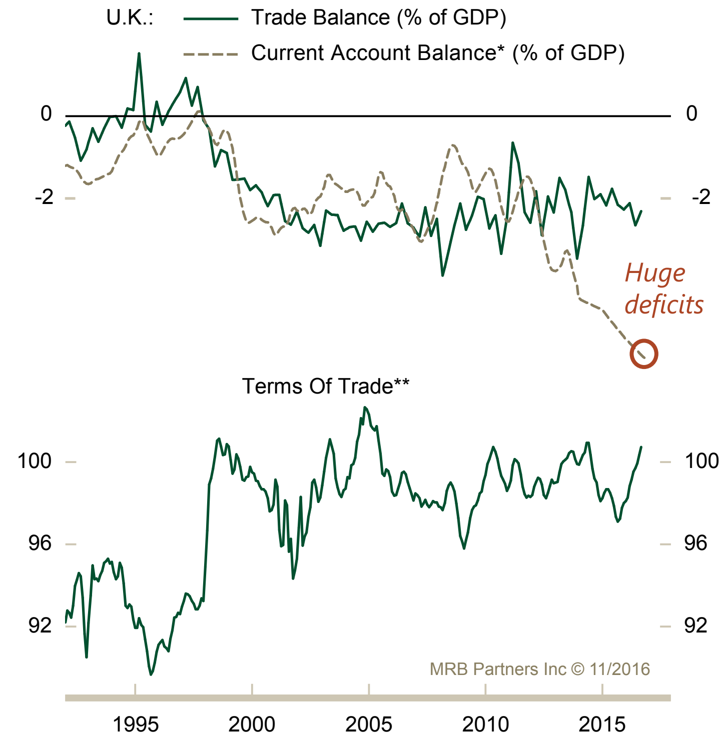
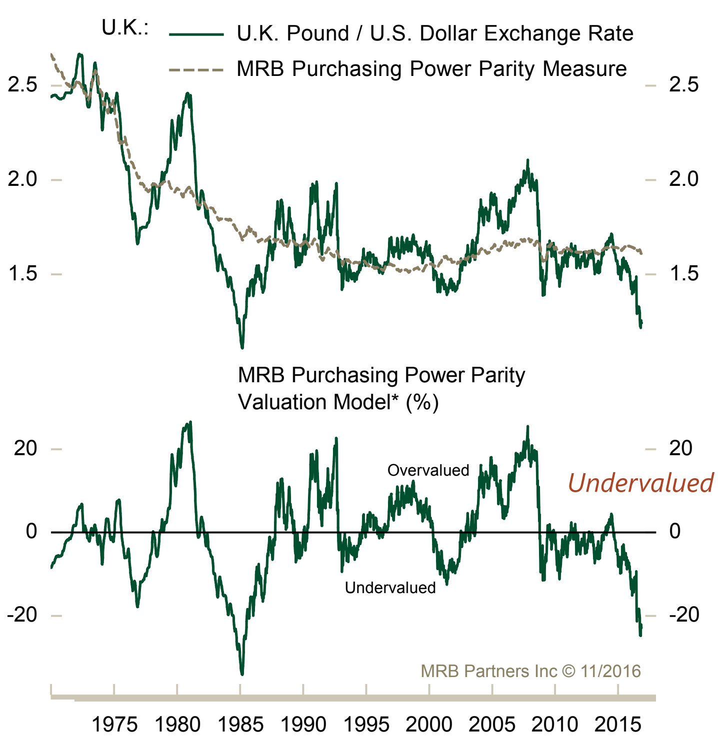
## Trade/Capital Flows



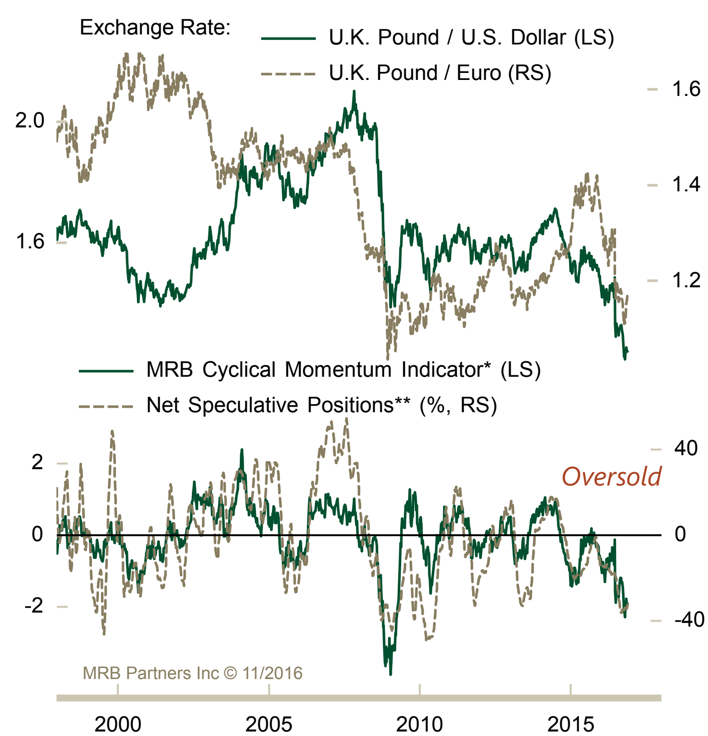

* Source: OECD
** Source: U.K. Office for National Statistics

## Valuation




* Percent deviation of currency from MRB Purchasing Power Parity Measure

## Technicals




* U.K. pound / U.S. dollar exchange rate; standardized
** Total long positions minus total short positions divided by open interest; smoothed; source: Chicago Mercantile Exchange

# U.S. Vs The Majors: *Overweight*

We highlighted in the October 28 MRB Weekly Macro Strategy Report that the USD would be a win/win bet from the U.S. election on a 6-12 month horizon. Although the USD is starting to become overbought, we expect further (albeit more gradual) broad-based upside.

**Relative Growth:** If president-elect Trump focuses on fiscal spending (rather than just tax cuts), this should help boost U.S. growth. Conversely, if he focuses on anti-trade policies, this is bearish for growth elsewhere, especially export-oriented economies. Either way, relative growth is likely to favor the USD in the near run. The longer-term outlook is darker as fiscal stimulus will be debt-fueled and anti-trade policies protect domestic inefficiencies. However, investors will not look that far ahead for now.

**Policy/Rates Differentials:** The Fed is likely to hike rates in December. While this is priced, interest rate differentials will still gradually move in favor of the USD as investors focus on further hikes in 2017.

**Trade/Capital Flows:** The U.S. still runs trade and current account deficits, and adopting protectionist policies is not a constructive or sustainable way to fix the external accounts.

**Valuation:** The USD is now overvalued according to the *MRB PPP Measure*.

**Technicals:** The USD is becoming overbought and speculators are already notably net long the currency. This will likely encourage the USD to consolidate somewhat before gradually edging higher.

**Final Word:** *Stay overweight the USD versus the majors on a 6-12 month horizon.*

**U.S. Foreign Exchange: Drivers Of Performance***

| | – | | N | | + |
|---|---|---|---|---|---|
| Relative Growth | | | | ■ | |
| Policy/Rate Differentials | | | | ■ | |
| Trade/Capital Flows | | ■ | | | |
| Valuation | | ■ | | | |
| Technicals | | ■ | | | |
| *Net Impact* | | | | ■ | |

* 6-12 month horizon; versus the major currencies
Note: + = positive, N = neutral, – = negative

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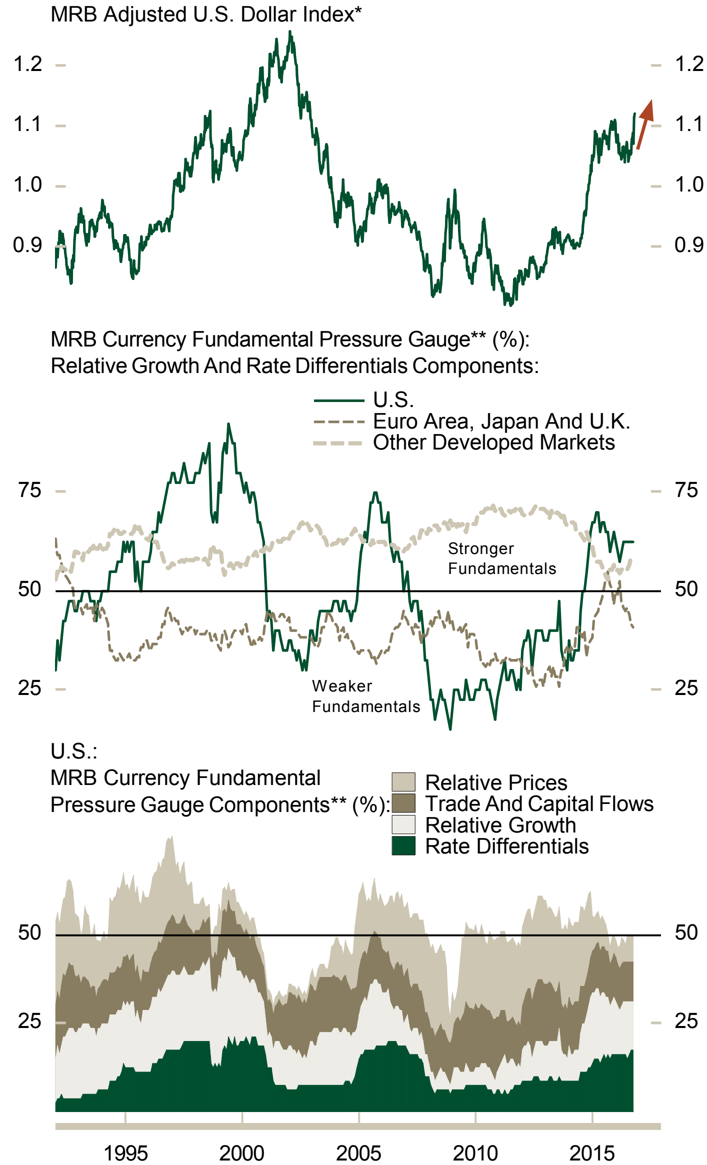
## Growth/Fundamentals




* Includes EUR (35%), JPY (26%), GBP (13%), AUD (10%), CAD (5%), CHF (5%), MXN (3%), and CNY (3%)
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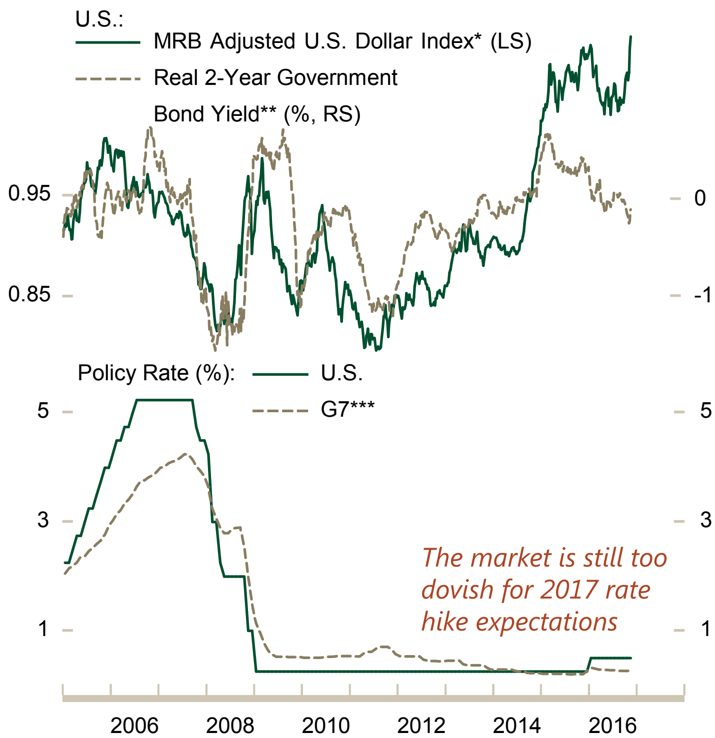
** Shown as a percentile ranking among developed markets

## Policy/Rate Differentials




* Includes EUR (35%), JPY (26%), GBP (13%), AUD (10%), CAD (5%), CHF (5%), MXN (3%), and CNY (3%)
** Deflated by headline CPI; U.S. minus G7
*** GDP-weighted aggregate

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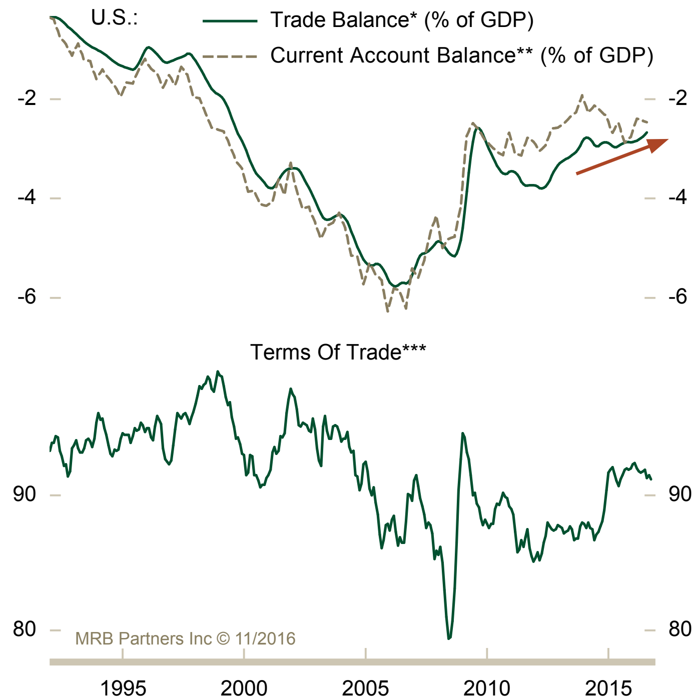
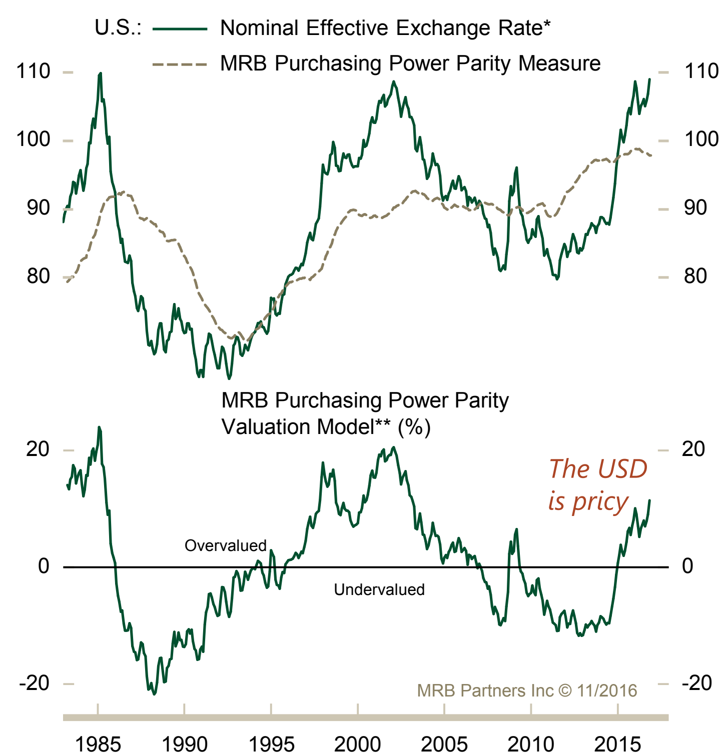
## Trade/Capital Flows



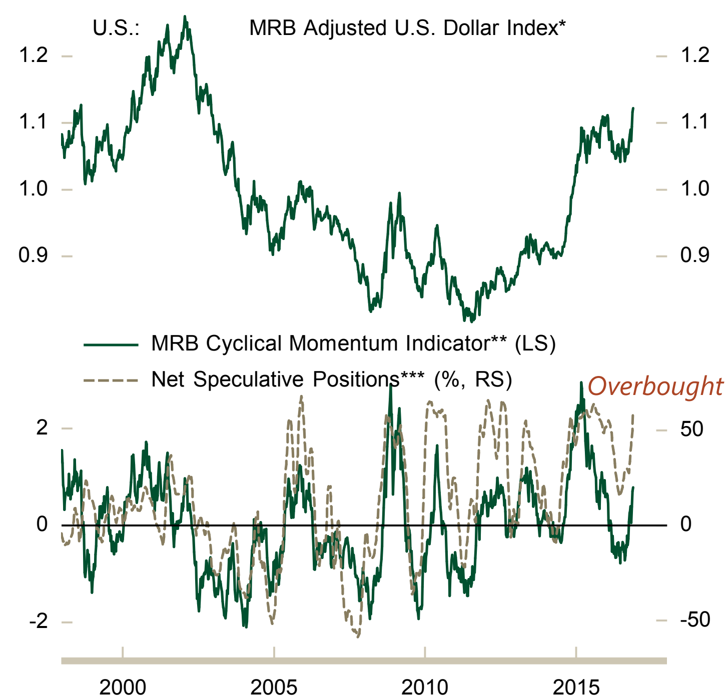

* 6-month moving average; source: OECD
** Source: OECD
*** Source: Datastream

## Valuation




* Source: J.P. Morgan Chase & Co.
** Percent deviation of currency from MRB Purchasing Power Parity Measure

## Technicals




* Includes EUR (35%), JPY (26%), GBP (13%), AUD (10%), CAD (5%), CHF (5%), MXN (3%), and CNY (3%)
** Standardized
*** Total long positions minus total short positions divided by open interest; smoothed; source: Chicago Mercantile Exchange

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# Emerging Markets: *Underweight*

Trump-related uncertainties associated with his many threats made against EM economies (including Mexico and China) during the electoral campaign cloud the outlook for EM currencies. We remain underweight EM currencies and would not bottom fish yet.

**Relative Growth:** Any move towards protectionism will be challenging for EM commodity currencies. Among EM currencies, we favor commodity importers over exporters as support from the bounce in natural resource prices (and easy liquidity) this year will fade. Also, currencies in economies with relatively limited export exposure and positive domestic growth drivers should hold up the best.

**Policy/Rates Differentials:** Interest rates in the overall EM complex will likely be lower, rather than higher in 2017. Colombia, South Africa and Turkey are the most susceptible markets to rate hikes as these economies need to attract foreign portfolio capital to finance external surpluses. However, such rate hikes will present economic headwinds, rather than being reflective of stronger growth conditions.

**Trade/Capital Flows:** Commodity importers enjoy current account surpluses and large foreign exchange reserves, which is supportive of these currencies. In contrast, weaker (or even range-bound) natural resource prices will be a drag on commodity-exporters' current account balances and foreign exchange reserves.

**Valuation:** Commodity-exporter currencies are slightly undervalued, while commodity importers are about neutral.

**Technicals:** Cyclical momentum measures suggest that currencies of commodity-importers are now oversold, while commodity-exporters are at neutral readings.

**Final Word:** *Stay underweight EM within a global currency basket. Among EM, favor emerging Asia.*

**Emerging Markets Foreign Exchange: Drivers Of Performance***

| | - | | N | | + |
|---|---|---|---|---|---|
| Relative Growth | | ■ | | | |
| Policy/Rate Differentials | | ■ | | | |
| Trade/Capital Flows | | | ■ | | |
| Valuation | | | | ■ | |
| Technicals | | | | ■ | |
| *Net Impact* | | ■ | | | |

* 6-12 month horizon; versus the U.S. dollar
Note: + = positive, N = neutral, - = negative
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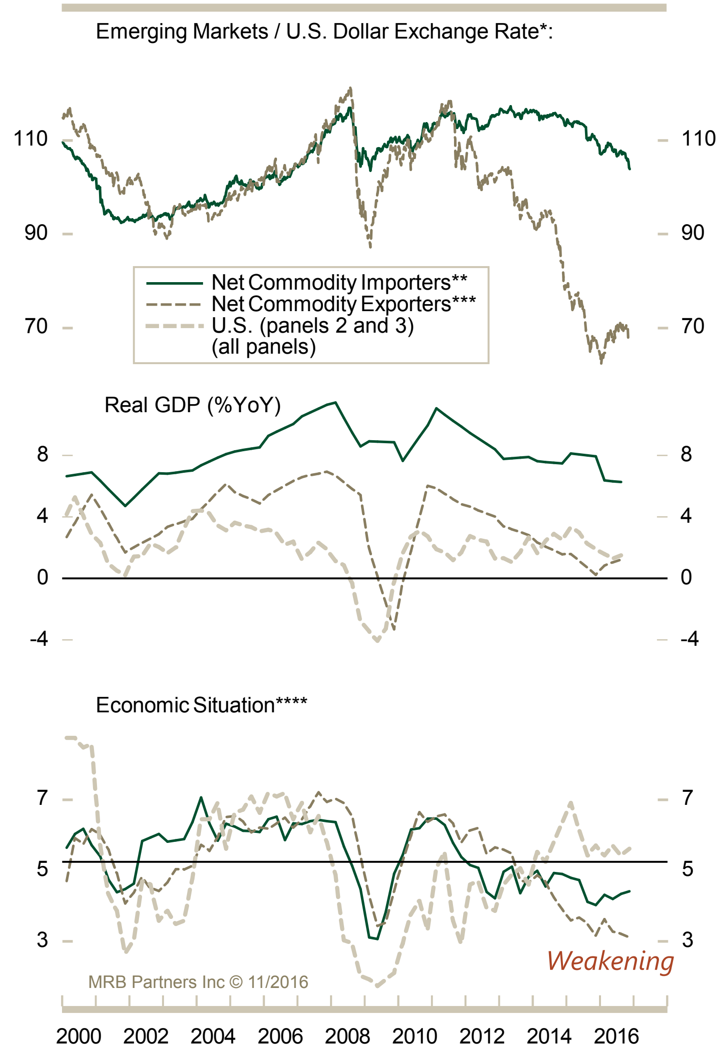
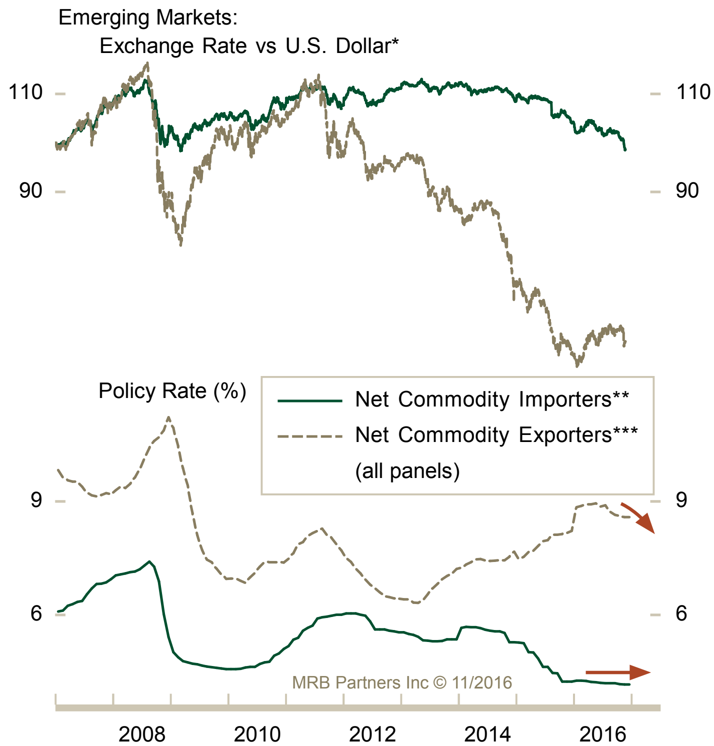
## Growth/Fundamentals



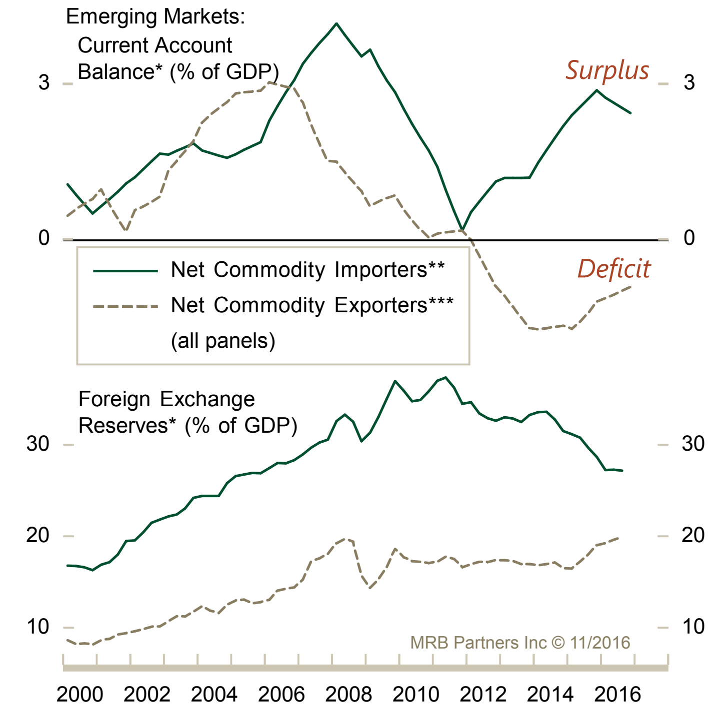

* Rebased
** GDP-weighted aggregate includes China, Czech Republic, Hungary, India, Korea, Philippines, Poland, Taiwan, Thailand and Turkey
*** GDP-weighted aggregate includes Brazil, Chile, Colombia, Indonesia, Malaysia, Mexico, Peru, Russia and South Africa
**** Survey ranges from 1 to 9; source: IFO Institute

## Policy/Rate Differentials



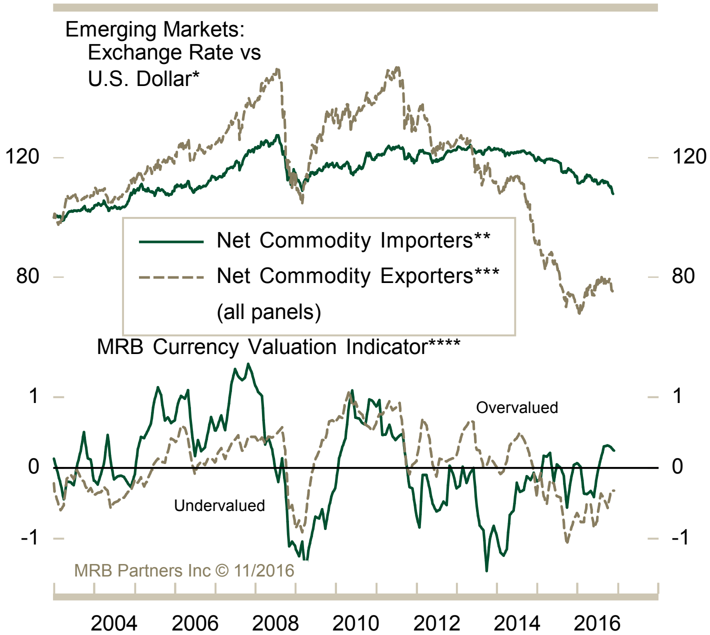

* Rebased; source: MSCI
** GDP-weighted aggregate includes China, Czech Republic, Hungary, India, Korea, Philippines, Poland, Taiwan, Thailand & Turkey
*** GDP-weighted aggregate includes Brazil, Chile, Colombia, Indonesia, Malaysia, Mexico, Peru, Russia & South Africa

## Trade/Capital Flows



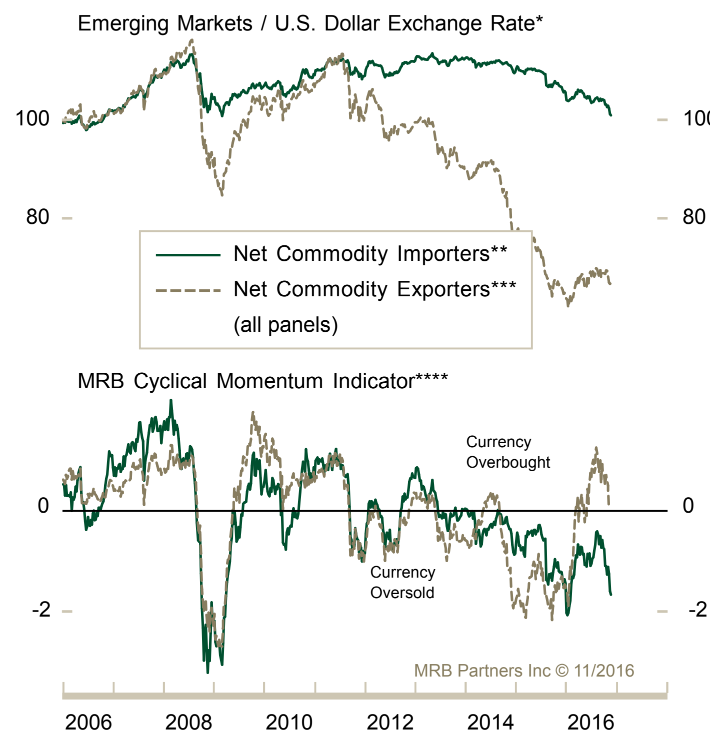

* Source: IMF
** GDP-weighted aggregate includes China, Czech Republic, Hungary, India, Korea, Philippines, Poland, Taiwan, Thailand & Turkey
*** GDP-weighted aggregate includes Brazil, Chile, Colombia, Indonesia, Malaysia, Mexico, Peru, Russia & South Africa

## Valuation




* Rebased; source: MSCI
** GDP-weighted aggregate includes China, Czech Republic, Hungary, India, Korea, Philippines, Poland, Taiwan, Thailand & Turkey
*** GDP-weighted aggregate includes Brazil, Chile, Colombia, Indonesia, Malaysia, Mexico, Peru, Russia & South Africa
**** Deviation from MRB Fair Value Estimate; standardized
Note: For panel 2 net commodity importers only include India, Korea, Turkey & Taiwan; net commodity exporters only include Brazil, Indonesia, Mexico, Russia & South Africa

## Technicals




* Rebased; source: MSCI
** GDP-weighted aggregate includes China, Czech Republic, Hungary, India, Korea, Philippines, Poland, Taiwan, Thailand & Turkey
*** GDP-weighted aggregate includes Brazil, Chile, Colombia, Indonesia, Malaysia, Mexico, Peru, Russia & South Africa
**** Standardized

November 25, 2016

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