



CIO maintains its Unattractive view on the US dollar and recommend investors to sell bouts of dollar strength to reduce exposure. (UBS)

Consider the potential impact of a depreciating US dollar on your portfolio

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The US dollar has strengthened further against its key trading partners amid rising Treasury yields, with the DXY index rallying to its strongest level since 2 August. This broad gauge of the US dollar's value against major trading partners' currencies has climbed 3.4% over the past month.

Recent economic data out of the US have been stronger than expected, reducing market expectations about the scope of Federal Reserve easing. CME FedWatch Tool data suggest a 91% chance of the Fed cutting rates by 25bps at its November meeting at the time of writing, compared to even odds priced a month ago of either a 25bp or 50bp cut in November. The increasing likelihood of former US President Donald Trump securing a second term has also added to the USD rally, as investors price for proposed tariff extensions under a new Trump administration, which are expected to add inflation pressures that keep US rates elevated.

However, we maintain our Unattractive view on the US dollar and recommend investors to sell bouts of dollar strength to reduce exposure.

The Fed remains set to lower rates amid lower inflation. Our view remains that the US central bank will continue to move toward a more neutral stance on interest rates amid broad disinflation, narrowing rate differentials with other G10 currencies. The most recent reading of the personal consumption expenditures price index (PCE), the Fed's preferred measure of inflation, showed annual inflation slowing to the lowest level since February 2021. Other inflation data for September, including producer price inflation, support our expectation of a further tick lower in the next release. For

example, shelter data, the biggest driver of inflation in recent times, appears to have finally turned around, which should help constrain overall inflation in the months ahead.

US fiscal concerns are likely to keep the US dollar under pressure. The US dollar could strengthen initially in the event of a second Trump administration, but we would expect that strength to eventually fade. Potential tariffs are likely to hurt US consumers and GDP more than the rest of the world, and deficit concerns may also surface with potential tax cuts. In fact, irrespective of who wins the presidency on 5 November, the growing US federal deficit is likely to come under the spotlight. A recent report by the Committee for a Responsible Federal Budget showed that the economic plans of both presidential candidates are forecast to swell US federal debt by trillions of dollars, while the Congressional Budget Office has projected that interest costs on US debt are set to exceed defense spending this year.

Other currencies should see additional support. On the other side of the Atlantic, we still expect a growth recovery in Europe going into 2025, with the European Central Bank advancing its rate-cutting cycle to support economic activity. Given the very downbeat sentiment on Eurozone growth, any positive surprises in data are likely to have a bigger impact on the euro than negative surprises. In addition, spillover effects from China's stimulus efforts and the potential for more risk-on sentiment after the US election should support other G10 currencies, including the euro, the British pound, and the Australian dollar.

So investors should consider the potential impact of a depreciating US dollar on their portfolios, and look to hedge dollar assets, switch USD cash and fixed income exposure into other currencies, and reduce exposure through options.

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Original report: [US dollar weakness should return, 23 October 2024.](#)

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