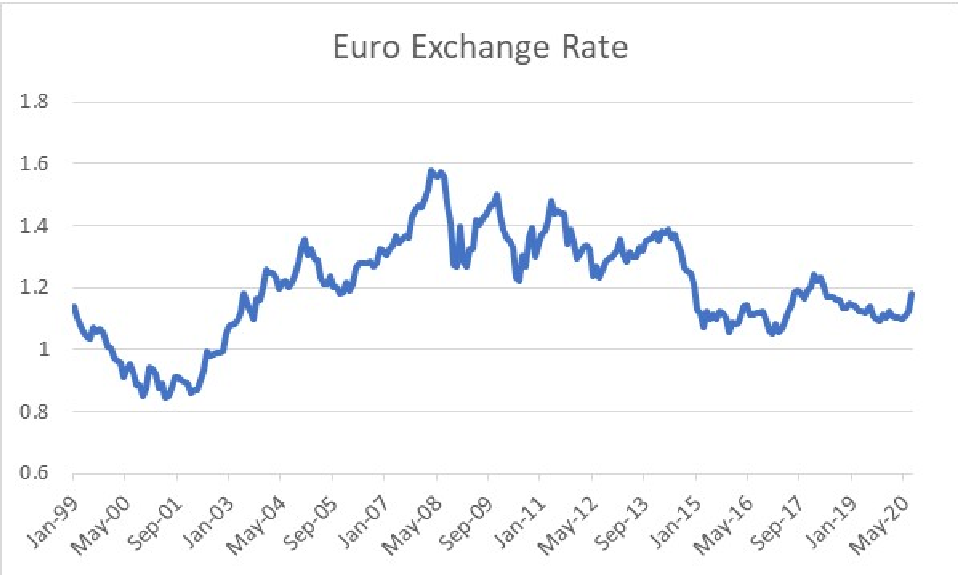
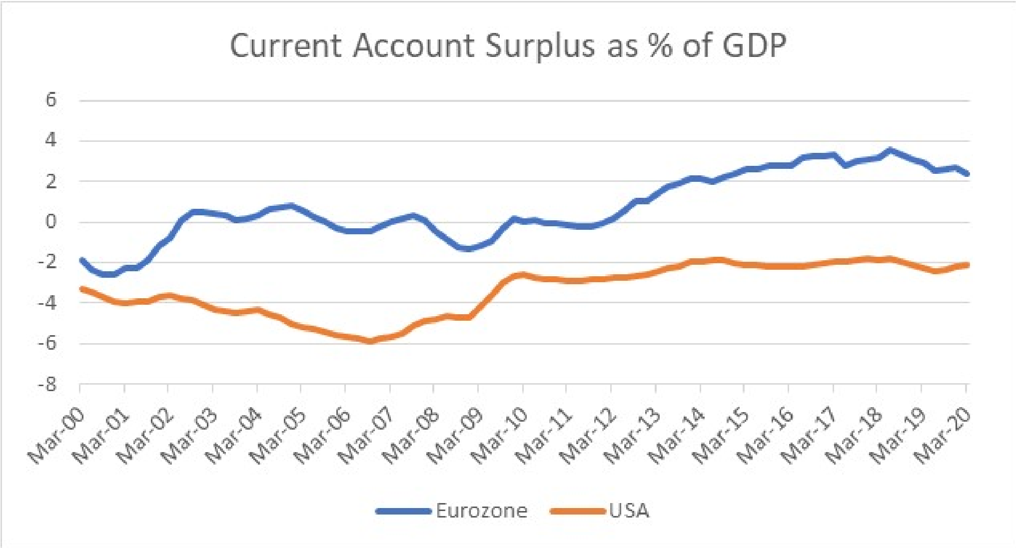
IS NOW THE TIME TO BUY EURO?

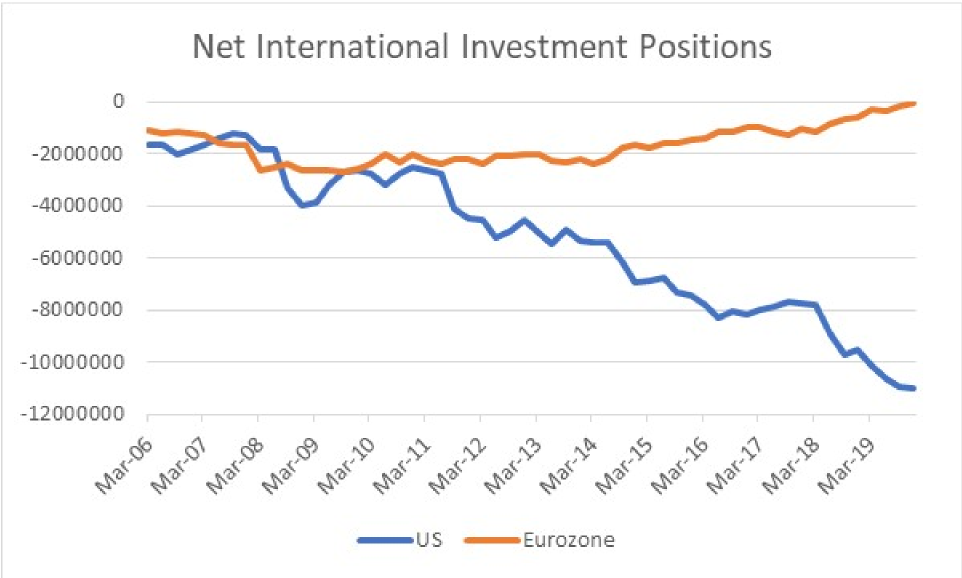
The Euro began life in 1999 at an exchange rate roughly the level it trades today, 1.18 to the US dollar.



Typically, the currency of countries that run a current account surplus tend to appreciate. Over this period, Europe has in general run a current account surplus, while the US has current account deficits.

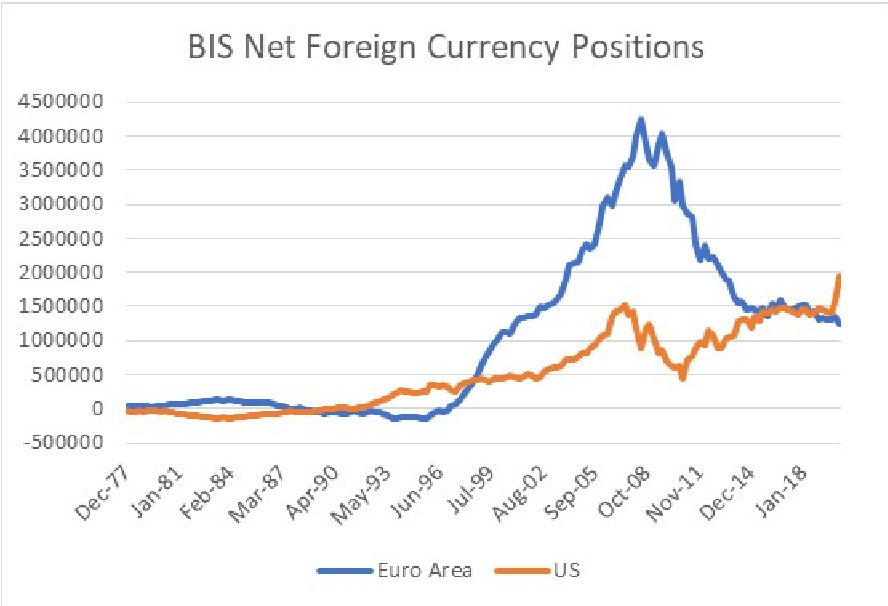


The Euro has not meaningfully appreciated over the time it has been running a current account surplus. Without the Euro appreciating, this had led to widely divergent net international investment positions. Narrowing of positions can be caused by falling asset prices, or changes in exchange rates.

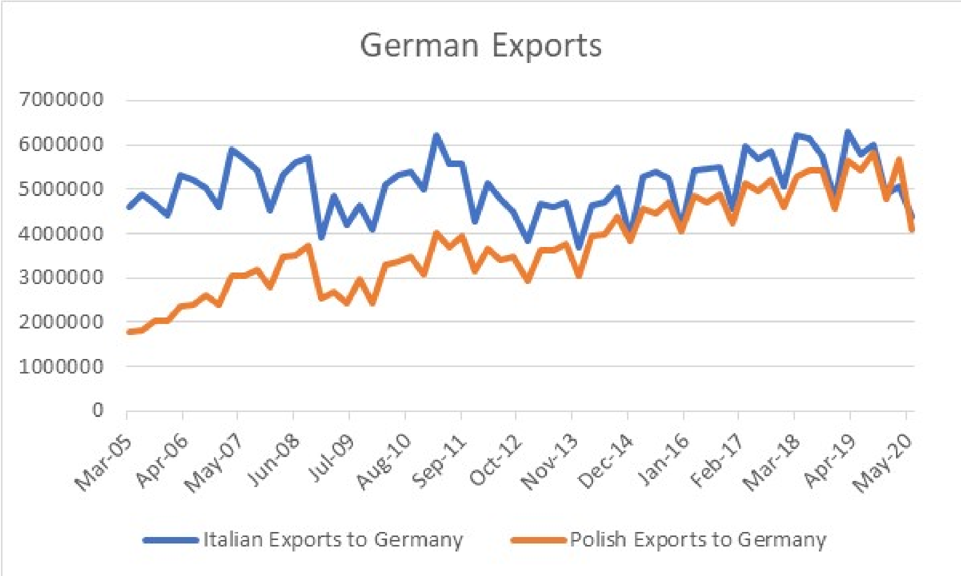


Another sign of the competitiveness of the Euro exchange rates is that despite tariffs and trade deals, the US trade position with China has continued to deteriorate dramatically, while Europe has broadly flatlined for the last 10 years.

The Global Financial Crisis, and then the Euro Crisis, caused credit flows to leave both the US financial system and the European financial system. Looking at BIS data, we can see that those credit flows have returned to the US but have not returned in Europe. This would make the US dollar more likely to fall relative to the Euro.

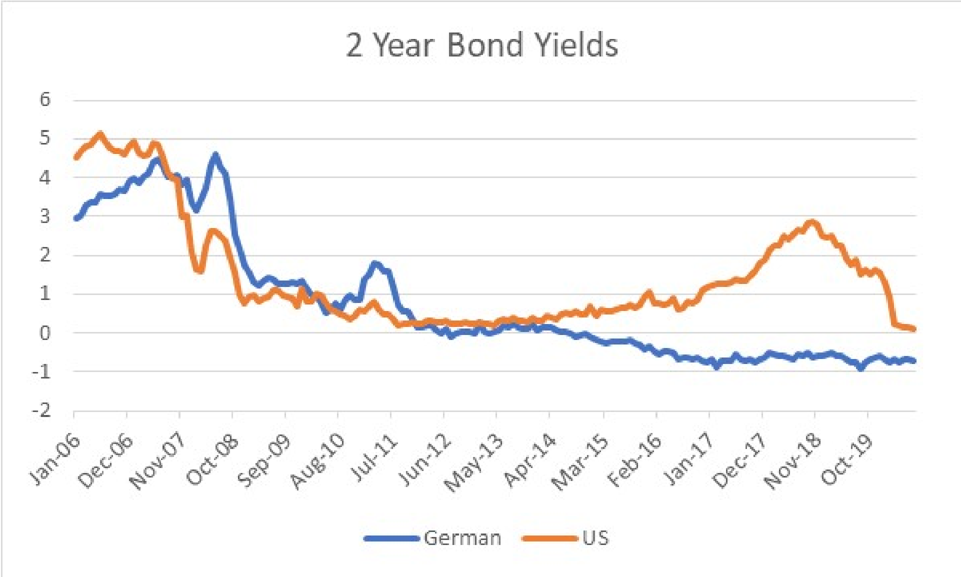


Many market commentators harbour a deep suspicion of the Euro. The main driver of this is a break up of the Euro, particularly the potential Italian exit from the EU. This has been driven by the very weak performance of Italy since the Euro was formed. While having a fixed exchange rate has made it impossible for Italy to devalue, another reason for Italian economic weakness was strong trade competition from Central European countries that joined the EU. As can been seen over the last 15 years, Italian exports to Germany flatlined, while Polish exports nearly tripled.



If we look at European exports to China, we can see that Italy has been able to grow exports to China to a degree. It has also increased its share of European exports to China, showing that higher wages in Eastern Europe have allowed Italy to regain some competitiveness.

Despite the fundamental data above that favoured the Euro, until recently US dollar investors would be compensated for these risks with substantially higher interest rates. The yield differential has fallen substantially.



The Euro looks set to appreciate against the US dollar.

INFORMATION

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