



While near-term dollar strength could persist, CIO believe investors should diversify their USD holdings, as the currency's strength eases over the medium term. (UBS)

Will the strong dollar persist?

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While the US dollar may stay well-bid in the near term, CIO believes its valuation may now be overstretched.

CIO recommends investors to use periods of strength to reduce US dollar exposure through strategies such as hedging dollar assets, switching USD cash and fixed income exposure to other currencies, and through options.

The US dollar has held on to its recent gains

- A second Trump term and Republican control of Congress have pushed the DXY index to the highest level since November 2022.
- While it has fallen from the November high, the index remains 5.6% higher since late September.
- Tax cuts and deregulation may attract capital inflows to US markets, while immigration controls could tighten the labor market, potentially keeping interest rates elevated. Tariffs might strengthen the dollar.

But short-term dollar strength should give way to renewed USD declines

- The DXY Index is trading out of line with its historical pattern versus 10-year US Treasury yields—at around 106, it is overshooting the yield-implied 105 level.
- Markets appear to underestimate Fed cuts by end-2025 while overestimating Eurozone rate reductions.
- Worries about the US government debt trajectory or unpredictable foreign policy could undermine confidence in US Treasuries as a safe-haven asset.

We like generating yield, reducing dollar exposure, and hedging with gold and USDCNY positions

- We see near-term opportunities to generate income in currencies, especially selling the risks of falls in the EURUSD and the GBPUSD, and the risks of a rising USDCHE.

- Investors with excess US dollars should use periods of dollar strength to hedge dollar assets and switch cash and fixed income exposure to other currencies.
- Gold prices and the USDCNY should rise in an adverse trade-war scenario where US tariffs surpass expectations and dampen Chinese GDP growth.

Did you know?

- USD strength following Trump's 2024 victory echoes the 2016 experience, but the DXY ultimately declined over the duration of the Trump presidency.
- The market expectation for around 150bp of European Central Bank easing by the end of next year looks too aggressive compared to our expectation for 125bp of rate cuts.
- During the 2018-19 trade spat, the USDCNH exchange rate rose around 11% between 15 June 2018 and 3 September 2019, as the US imposed tariffs on Chinese goods in a staggered manner.

Investment view

While near-term dollar strength could persist, we believe investors should diversify their USD holdings, as the currency's strength eases over the medium term. We like the Swiss franc, the euro, the British pound, and the Australian dollar. We also recommend an allocation to gold of up to 5% within a balanced USD portfolio.

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Original report - [Will the strong dollar persist?, 9 December 2024.](#)

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