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# Is the strong-dollar era over?

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**All told, while the U.S. dollar might soften modestly from here, it will soften unevenly against major global currencies.**

The relative strength and direction of the U.S. dollar matters: trade balances can fluctuate, multinational corporations can see foreign sales rise or fall and U.S. dollar-denominated investors in international markets can see returns amplified or diminished. Understanding how the dollar might move is therefore important, and after years of appreciation, the dollar has swiftly declined, off about 5% from its peak earlier this year. As a result, many investors might wonder: is the strong-dollar era over?

Interest rate differentials are a key piece of the puzzle: the gap between global central bank policy rates can change the relative attractiveness of local-currency debt instruments, and investor appetite for this debt can then drive its related currency higher or lower.

In this context, dollar strength makes sense: central bank hiking cycles post-pandemic were, after all, not of the same magnitude. The Federal Reserve took the overnight rate to 5.25 - 5.50% while other central banks hiked with varying intensity: the Bank of Canada (BoC) and Bank of England (BoE) nearly matched the Fed with peak policy rates of 5.0% and 5.25%, respectively; the European Central Bank (ECB) lagged modestly at 4.0%; and the Bank of Japan (BoJ) trailed far behind at 0.25%.

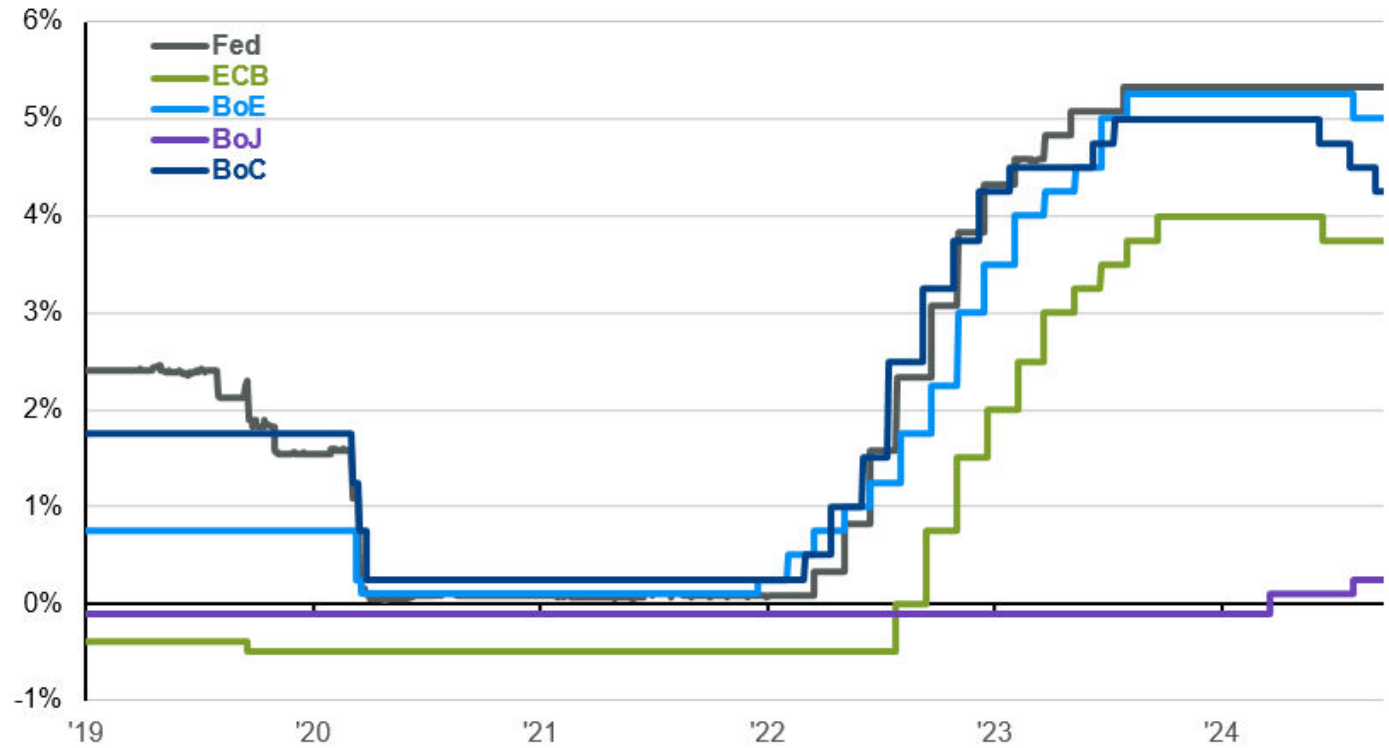
More recently, unequal and uncertain central bank policy "normalization" has complicated this dynamic: the BoC, ECB and BoE all began their cutting cycles earlier this year with varying intensity; the BoJ continues to hike, eager to keep rates positive without crushing inflation; and the path of future Fed cuts remains dependent on incoming economic data (the September "dot plot" shows the Fed cutting by about 100 bps total this year, while the future's market is pricing in a more dovish 125 bps).

As a result, rate differentials might not compress as much as is currently priced into the dollar, potentially challenging the recoveries for the euro, pound and Canadian dollar and suggesting that the recent yen rally (up 12% so far this quarter) might be tapped out.

All told, while the U.S. dollar might soften modestly from here, it will soften unevenly against major global currencies. Still, relative dollar stability is a departure from the strong gains experienced over the last several years and should be seen as a positive development, resulting in more predictable foreign sales from U.S.-based multinationals (particularly those with large exposures overseas, like Technology and Materials) and a purer return experience for U.S. investors in foreign markets.

# Diverging monetary policies among major central banks

Policy rate, percent



Source: Bank of Canada, Bank of England, Bank of Japan, European Central Bank, Federal Reserve, FactSet, J.P. Morgan Asset Management. ECB announced a reduction in policy rate to 3.5% on Sep. 12, 2024, however, the change will be effective from Sep. 18, 2024.

Data are as of September 17, 2024.

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