JULY 17, 2023

PHILEQUITY CORNER

By Wilson Sy

Dollar breakdown

As defined by Investopedia, a breakdown is a downward move in a security or currency's price, usually through an identified level of support, that portends further declines. This aptly describes the recent move of the US dollar index (DXY) as it pierced through its technical support level of 101 and the round-number support of 100. The recent dollar breakdown came amid reports of easing US inflation which spurred market expectations that monetary tightening is in its final stages.

Significant turning point

In one of our previous articles, we discussed notable reversal moves in various asset classes which took place in October last year (see *Peak dollar*, October 31, 2022). We wrote: "The US dollar index reversed, generating dramatic moves that day for FX, rates, bonds, and stocks –and marking a significant turning point." The price action across asset classes last October signaled a bottom for stocks and a peak in the US dollar. The S&P 500 is up 29% while DXY has fallen 10.8% since October 21.

US dollar index (DXY)

Reversal in currencies

The breakdown of the US dollar last week drove strong reversal moves in currencies worldwide. The euro broke out, gaining 13.9% since October 21 and 4.9% year-to-date. The British pound and Swiss franc are up year-to-date and have posted double-digit gains since the start of the dollar reversal.

Major currencies	Year-to-date	Return since Oct 21
British Pound	8.3%	15.8%
Swiss Franc	7.3%	15.8%
Canadian Dollar	2.6%	3.2%
Euro	4.9%	13.9%
Norwegian Krone	-2.5%	4.8%
Japanese Yen	-5.5%	6.5%

Asian currencies have likewise advanced with the US dollar's decline. The peso has been one of the best performers in the region with a gain of 8.1% since October 21 and 2.6% year-to-date.

Asia-Pacific Currencies	Year-to-date	Return since Oct 21
Indonesian Rupiah	4.1%	4.5%
Philippine Peso	2.6%	8.1%
Singaporean Dollar	1.3%	7.1%
Australian Dollar	0.4%	7.2%
Indian Rupee	0.9%	0.8%
Thai Baht	-0.1%	9.7%
Taiwanese Dollar	-0.7%	4.0%
Korean Won	-0.6%	13.6%
Chinese Yuan	-3.4%	1.3%
Malaysian Ringgit	-2.6%	4.8%

Easing inflation, peak rates bode well for market

Data released last week showed that US inflation slowed to 0.2% MoM and 3% YoY, the lowest since March 2021. This signaled that inflation is on a downtrend. Investors now hope that the Fed will just raise once instead of twice, as indicated in the Fed's latest dot plot. A peak in interest rates would lower the risk of recession due to overtightening. Expectations of peak rates triggered the latest breakdown of the US dollar, and this spurred the strong rebound of most currencies, including the peso. Overall, the continued easing of inflation and a peak in interest rates are bullish signals for global currencies and most asset classes.

Start of new PSEi bull market

The strong move of currencies is bullish for stock markets. S&P 500 is up 17.3% year-to-date while EEM is up 8.2%. The PSEi was in the red for a good part of the year. However, it is now up 0.9% year-to-date after rising by 3.9% last week. The Philippine market saw a return of foreign buying (P2.6b net inflows last week) after experiencing net outflows in the past six weeks. Market volume rebounded (P4.5b average daily value traded last week) after dipping to the lowest levels in recent memory (P2b to P3b levels for July 3 to 7). The streak of foreign selling and historically low trading volume indicated extreme bearishness and total disinterest for the Philippine market. Based on technical analysis, extremely low trading volume typically ushers the bottoming-out of bear markets. In this light, the US dollar breakdown, the imminent end of interest rate hikes, and the PSEi's revival last week may be signaling the start of a new bull market for Philippine stocks.