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STRATEGIES FOR SUCCESSFUL INVESTING

MARKET WISDOM

The U.S. Dollar

A POSSIBLE HEDGE

Keith Richards

LOONS FLY NORTH FROM THEIR southern retreats as Spring approaches. So too do Canadian retirees known as “snowbirds”. The Canadian dollar, affectionately known as the “loonie”, follows that same desire to fly north as the weather begins to warm. Our friend Jon Vialoux over at www.equityclock.com presents this seasonal chart for the CDN\$ - as seen on the next page. Notice how the single best time to be long the loonie is from its seasonal low point in February into its seasonal high point in mid-June.



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That's about 2 months away from the time of writing this article. But you'll also note that the biggest upside has occurred by the end of April. By the time you read this article, that time period will have arrived. According to the seasonal patterns of the CDN\$ vs. the USD, the loonie will already have peaked.

It most certainly does appear that the loonie is following its traditional, seasonal-northern flight this year. Having bottomed at just over \$0.76 in March, it is currently sitting well over \$0.79/USD. Take a look at the long-term chart below. The loonie frequently likes to trade in a range between \$0.78 - \$0.83. I suggested back in early March on my blog at www.vvaluetrend.ca that there might be a reasonable chance for the CDN\$ to move back into that trading range by the Spring - despite the

bigger problems we face as a country of current rising debt, increased taxation and an unfavorable business environment under current left wing governments.

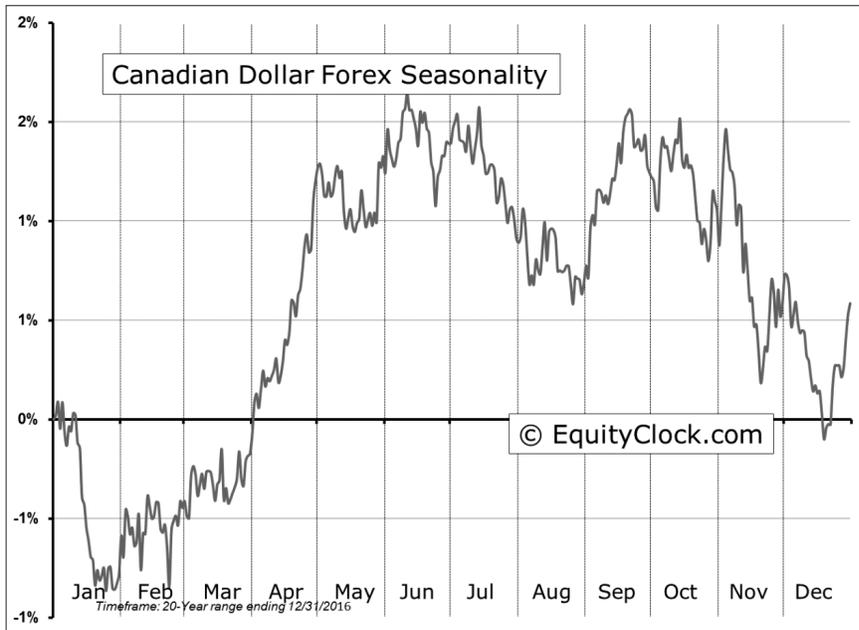
On the chart at the top of the next page, you'll notice that another near-term downtrend began in the second half of last year. We are currently approaching the top of that downtrend. A glance at the chart on the bottom of the page suggests a target of about \$0.80 before we challenge the top of this trend channel. As I noted in my blog in March, my target was \$0.80. We're now less than a penny away from this target, which resides along the top of the minor-trend channel. Before we get too excited, there is some compelling evidence suggesting that the current rally in the loonie may be short-lived.

Sentiment speaks

As you may know, the USD - against a basket of world currencies - has been trending down over the past year or so. In fact, www.sentimentrader.com posts a “USD Optix,” which is a compilation of sentiment indicators pertaining to the USD. The Optix suggests that the USD has overly bearish sentiment. And that, as you may know, is a contrarian Buy signal. Too much pessimism on any asset class tends to reverse itself after reaching an extreme. And that reversal in sentiment typically results in money flow into the currently depressed asset.

Should the USD begin to move up when sentiment reverses, the movement will add pressure to an already vulnerable position for the Canadian loonie. The chart below – courtesy of Sentimentrader, marks the Buy zone as below the lower horizontal line, and the Sell zone as above the red horizontal line. The USD is indicated by a black line above the Optix indicator. I've circled times where the Optix was above or below the horizontal lines. Notice how the USD tends to rise when the Optix stays below the lower horizontal line for too long, and the USD falls when the Optix stays above the upper horizontal line. The current move below the buy-zone suggests that bearish sentiment is overdone – an occurrence that has historically coincided nicely with bullish reversals on the dollar.

Further to that potential...the USD has a negative correlation with the stock market. The USD rises when stocks fall more often



than not. I discussed this on a blog at my website noted above. If you believe, as I do, that there is reason for a substantial market correction this year, this would add fuel to a rising USD.

My strategy

As I have noted in the past, I will be converting more financial

assets into USD as/if/when we see the loonie reach \$0.80 – or thereabouts. That time is approaching as I write this article.

As discussed above, chart patterns on the CDN\$, along with sentiment data and a stronger outlook for the USD, suggest that the loonie will finish its northern flight sooner rather than later. You



might consider holding some USD exposure in your own portfolio should that trade come to fruition. If nothing else, it might be a bit of a hedge against a stock market decline. ▼

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