The ‘Grand Old Party’ and the U.S. dollar
by Howard Friend C.M.T.

The storming of the White House by Donald Trump last November created not just the usual ripples on a change in U.S. leadership but many shockwaves both at home and abroad as the world holds its breath waiting for the ‘New Normal’ to emerge.

For those trying to get a handle on what to expect over the next four or more years the early months of the Presidency have been a little perplexing to say the least. Differences have emerged between Mr. Trump’s isolationist pre-election rhetoric and some of his actions in the Oval Office, particularly in the field of foreign policy which has seen unilateral action in Syria, strong assurances given to NATO and the ramping up of stakes with North Korea.

Despite all the confusion and contradictions witnessed so far it is worth pointing out that while in what used to be called ‘the free world’ the leader of the elected political party holds a very large amount of sway over government policy, he or she will still need a groundswell of support to retain power. This involves consensus-building and compromise with the various power brokers within the ruling party which inevitably leads to some dilution of the power of the president relative to the party.

Assuming the ‘party over president’ theme holds true in this case and that the core values of the Republican party are to dominate the major policy decisions going forward I thought it would be a worthwhile exercise to review the historical performance of the U.S. dollar during various Republican administrations to see whether there were any common themes which could affect the value of the currency. Here’s what I discovered.

Since Nixon’s landslide victory and inauguration in 1969 there have been eight U.S. presidents prior to the current incumbent. I list them here along with the accompanying percentage change in the dollar as measured by the U.S. dollar exchange rate verses the Euro since inception in 1999 and its constituent parts prior to inception.

U.S. Presidents (1969 to 2017)

Richard Nixon (January 1969 to August 1974) : Percentage change in U.S. dollar: -16.23%

Gerald Ford (August 1974 to January 1977) : Percentage change in U.S. dollar: +2.23%

Jimmy Carter (January 1977 to January 1981) : Percentage change in U.S. dollar: -10.28%

Ronald Reagan (January 1981 to January 1989) : Percentage change in U.S. dollar: +9.79%

George H.W. Bush (January 1989 to January 1993) : Percentage change in U.S. dollar: -8.68%

Bill Clinton (January 1993 to January 2001) : Percentage change in U.S. dollar: +30.80%

George W. Bush (January 2001 to January 2009) : Percentage change in U.S. dollar: -29.13%

Barack Obama (January 2009 to January 2017) : Percentage change in U.S. dollar: +24.72%

Here is a chart courtesy of FXtop.com which highlights the trend in the currencies of the Eurozone against the U.S. dollar from the late-1960s to date.

Source: FXtop.com

The chart shows a slight upward bias in the trend (downward bias for the USD) since 1985 when the G5's Plaza Agreement halted the steep rise in the value of the dollar seen during the early Reagan years. While the bias has on balance been for a lower dollar over the whole period it is worth noting that there have been a number of significant price swings of large duration which provided opportunities for the global macro investor. Note that the decline (U.S. dollar advance) which has been in effect since 2008 has held above the trendline coming in from the 1985 and 2000 lows - a positive sign for the market technicians among us.

Putting these price swings into the context of who was in the White House at the time a very interesting fact stands out. **The dollar has tended to fall when a Republican has been the incumbent** with three out of the five Republican presidents presiding over a decline in the currency while only one of the three Democratic presidents (Carter) at the wheel while the dollar fell.

Taking a closer look at the numbers and counting the full terms of the ruling parties sheds some more light on what could be an inherent 'bias' towards the currency dependent on which party has been elected. I list the administration by party and changes in the value of the dollar below:

U.S. dollar: percentage changes by political party (1969 to 2017)

REPUBLICAN: Nixon and Ford (January 1969 to January 1977)

Percentage change in U.S. dollar: -14.37%

DEMOCRAT: Carter (January 1977 to January 1981)

Percentage change in U.S. dollar: -10.28%

REPUBLICAN: Reagan and Bush (January 1981 to January 1993)

Percentage change in U.S. dollar: +0.26%

DEMOCRAT: Clinton (January 1993 to January 2001)

Percentage change in U.S. dollar: +30.80%

REPUBLICAN: G.W. Bush (January 2001 to January 2009)

Percentage change in U.S. dollar: -29.13%

DEMOCRAT: Obama (January 2009 to January 2017)

Percentage change in U.S. dollar: +24.72%

The 1970s were not a good time to be holding U.S. dollars under administrations of any stripe. The decline which followed Nixon's departure from the stability of the Bretton Woods Agreement saw a net loss for the combined Republican term at 14.37% which was extended under Carter before Reagan and monetarism saved the day, halting the inflationary spiral which had dogged monetary policy during the 1970s. Apart from the fact that Nixon abandoned the stability of a 'pegged' exchange rate in favour of a floating (or sinking) currency, no major party political biases were apparent until the latter half of the 1980s.

Things started to become clearer during Reagan's second term and into Bush senior's sole term as the dollar saw a complete reversal in its post-Plaza Accord advance by the time the Republican triple-term had ended in 1993. Some might say that the next president, Mr. Clinton, may have benefitted from a 'peace dividend' as an extended period of global stability unfolded following the end of the Cold War which may have contributed to the first sustained period of strength under a Democratic President. The U.S. unit ended his scandal-hit second term some 30% higher than where he found it eight years prior.

The Clinton Presidency gave way to a less sanguine era in which George W. Bush gifted the world with a post-9/11 "with us or against us" consensus which saw the controversial involvement in Iraq and the 2008 financial crisis. Looking through the rear view mirror it may come as no big surprise that the dollar ended nearly 30% lower at the end of his tenure but could it have been a case of returning to type under another long period of Republican control?

The third successive 20% plus move in the U.S. unit occurred under Mr. Obama who had to adopt many of the foreign policy stances of his predecessor whilst fighting the fires of the financial crisis. While government finances continued to deteriorate the fact that confidence slowly ebbed back into the financial system after the meltdown along with a broad disengagement from far away wars and combined with woes in the Eurozone may have helped to put a floor under the greenback.

Despite all of the major events on the world stage which have occurred since the end of the 1960s, which conventional wisdom would argue for a stronger or weaker US dollar the facts are as follows:

REPUBLICAN presidential terms have seen an average DECLINE in the US dollar of 14.41%

DEMOCRATIC presidential terms have seen an average RISE in the US dollar of 15.07%

A good case for a bearish turn in trend?

Regardless of whether one believes that movements in the value of the U.S. dollar or the Euro for that matter are dependent on external shock events (Rumsfeld's "unknown unknowns") or indeed the policy decisions of those in power who are guided by their own collective political persuasions, it is worth noting that financial markets often appear to have a 'life of their own.

As with most things in life there are often long-term trends and cycles at work which have a strong pull on prices over time which can create logic defying price movements. Of note in this case is the fact the six price swings I have highlighted have shared similar characteristics in terms of extent in particular in terms of duration which begs the question: Where could we be in the current cycle? Here are the average price swings from 1969 to 2016 along with details of each price swing:

Average percentage change: 67.24%

Average duration: 94.83 months (7.9 years)

August 1969 to October 1978: Duration: 110 months, percentage change: -36.08%

October 1978 to February 1985: Duration: 76 months, percentage change: +130.15%

February 1985 to September 1992: Duration: 92 months, percentage change: -57.39%

September 1992 to October 2000: Duration: 97 months, percentage change: +77.14%

October 2000 to July 2008: Duration: 93 months, percentage change: -48.39%

July 2008 to December 2016: Duration: 101 months, percentage change: +54.28%

As at the time of writing (25th April 2017) the Euro/US dollar exchange rate is trading around the 1.0900 level having found support in the 1.0300-1.0500 region following the 2014/2015 slide which completed the larger decline (U.S. dollar advance) from the 2008 peak. This begs the question: Could the last major up cycle for the U.S. dollar have run its course? A comparison with the extent and duration numbers seems to point in that direction as the last U.S. dollar uptrend had been in effect for 101 months (versus 94.83 months) at the December 2016 U.S. dollar peak while the extent number of +54.28% fell a little short of the 67.24% average price movement but was well within the historical range.

Conclusion

While the political, economic and cyclical drivers which ultimately produce the large trends in asset prices can often be at odds with each other at least two of these dynamics have in my view created a ‘perfect storm’ for the U.S. dollar. Republican governments have tended to coincide - either by accident or by design - with a falling currency while the U.S. dollar has actually been rising (EUR/USD falling) for longer than its historical average term which suggests a **very high risk of seeing a much lower U.S. dollar over the next few years.**

While the Eurozone will undoubtedly have its own problems to contend with not least keeping the bloc together post-Brexit my guess is that whatever may be in store for the U.S. over the Trump presidency could be (or more importantly, perceived to be) relatively worse than the issues facing Europe. For those who are in the business of forecasting currency rates this is the salient point as one currency is measured in terms of another as there are two sides to the equation.

Whatever the drivers of the impending under performance of the US dollar may turn out to be the paradox is that a weaker currency will ultimately provide a boon to Trump’s “America first” agenda as the so called “currency manipulators” will finally be brought to book courtesy of yet another competitive devaluation in the almighty U.S. dollar. Watch this space……

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