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Q1 2025 FX Market Outlook

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FX Markets Update

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- Dollar rallied across the board on:
  - US economy has been stronger than other DMs; China continues to suffer from its real estate sector
  - Higher interest rates in the US than in the rest of DM
  - US exceptionalism (Economic growth, Tech sector, capitalism)
  - Trump elections, which reenforced the above and created concerns about tariffs further hurting rest of the world
- JPY continues to have negative real yield
- BRL and KRW suffered due to their idiosyncratic issues

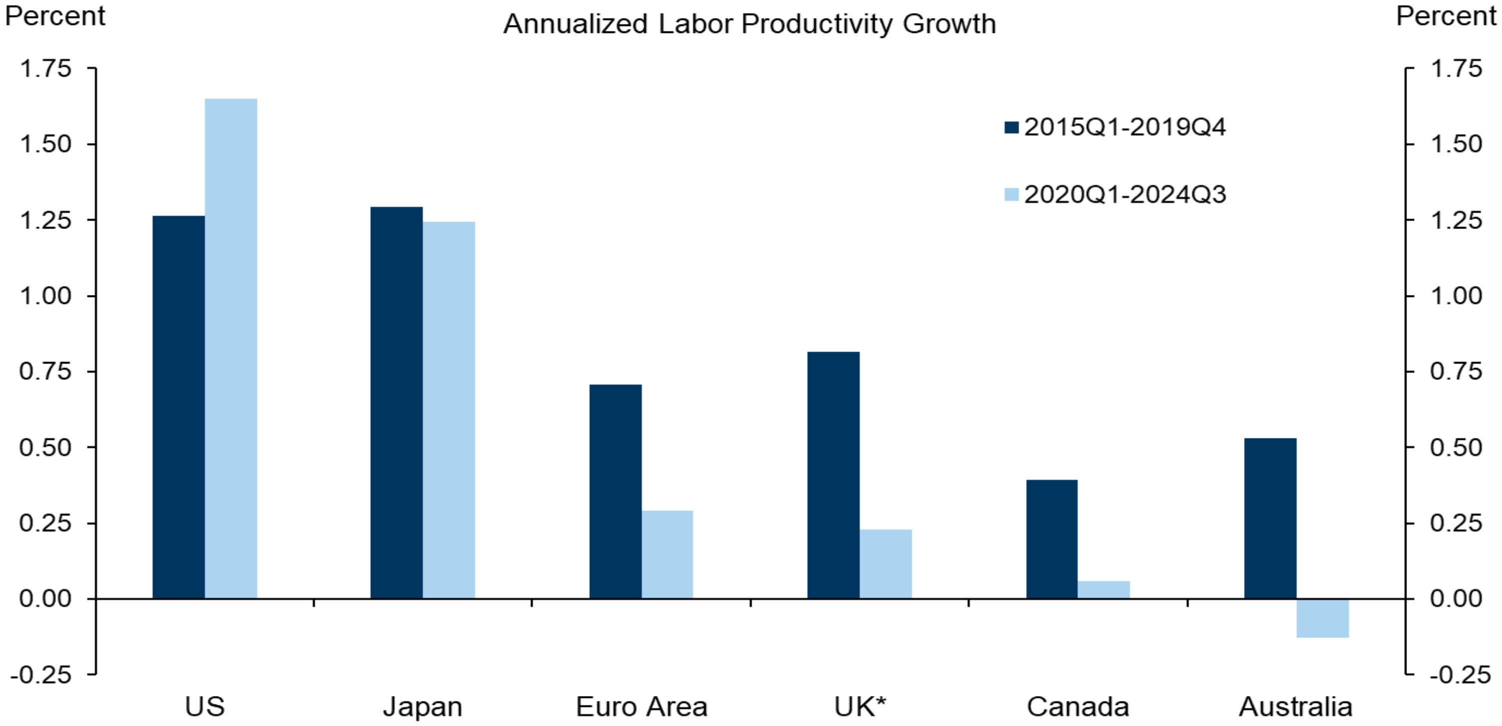
FX Performance as of Dec 31, 2024

	EUR	GBP	JPY	AUD	CAD	BRL	INR	KRW	MXN	ZAR
Q4 2024	-7.6%	-6.6%	-10.2%	-10.9%	-6.4%	-10.8%	-1.6%	-11.4%	-4.3%	-8.1%
2024	-8.0%	-2.1%	-15.4%	-10.3%	-9.0%	-18.1%	-0.9%	-14.0%	-13.5%	-0.3%

Source: Bloomberg, SECOR

US exceptionalism story

- US productivity has been much higher than in ROW, particularly post-COVID
- Higher productivity and technological innovation supported stronger growth and stronger stock market
- This, in turn, resulted in strong cross-border flows in the US



Note: Labor productivity is defined as total-economy real value-added per hour worked.
* UK 2024Q3 productivity is a GS forecast.

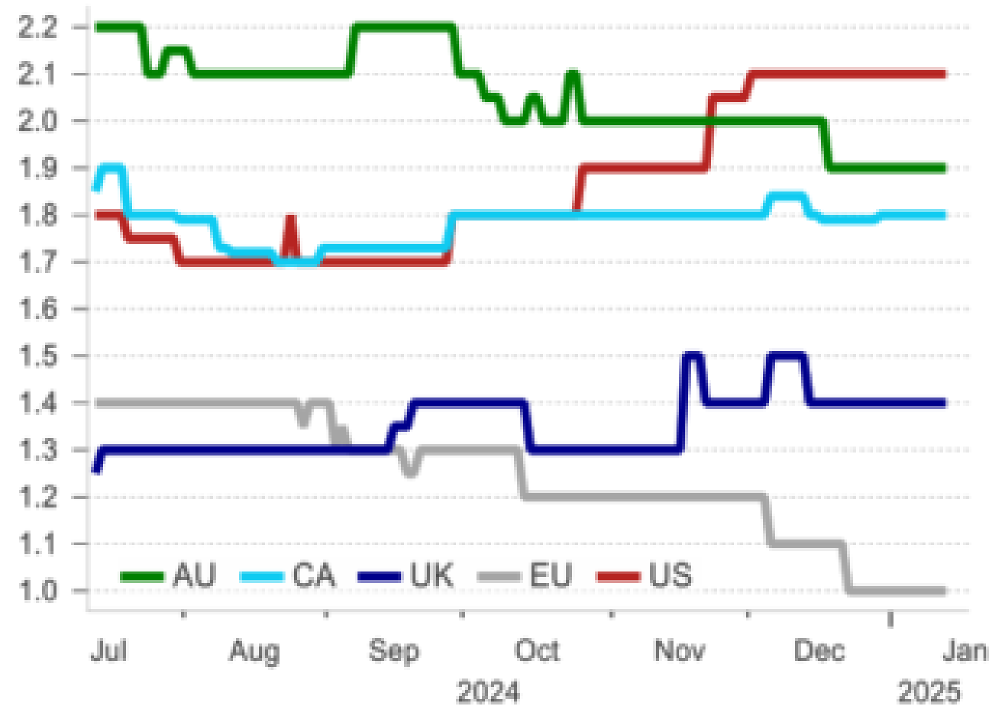
Source: Goldman Sachs

Macro Drivers of FX Performance

- Interest rates and changes in economic forecasts have been USD supportive

Figure 5: Economists have revised up US growth expectations for this year

2025 median growth forecast in %



Source: Bloomberg, Nomura

FDI and Portfolio Flows have been USD supportive

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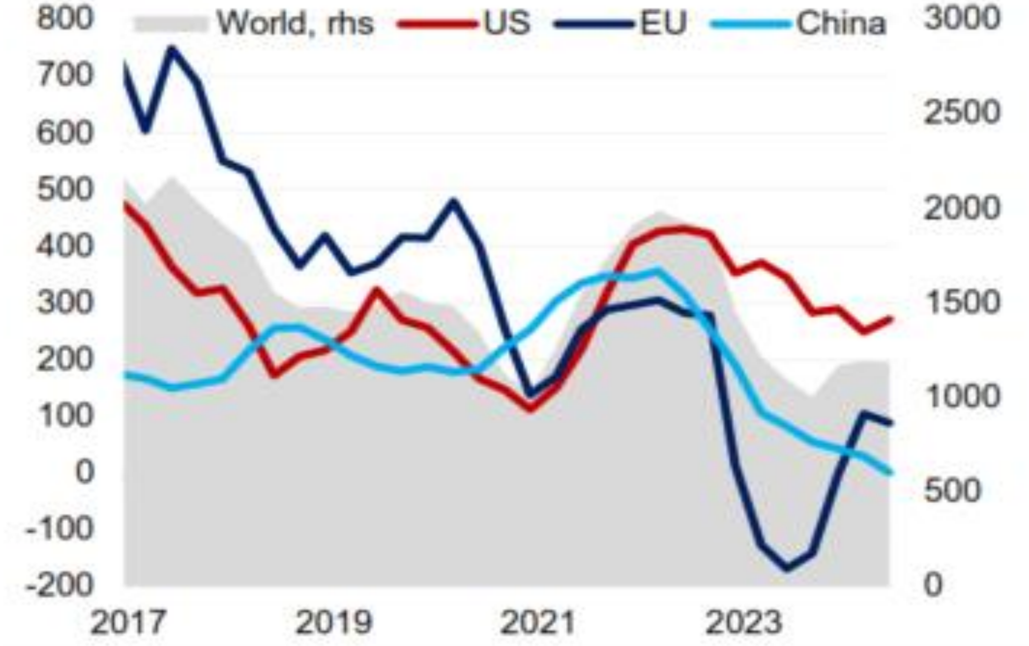
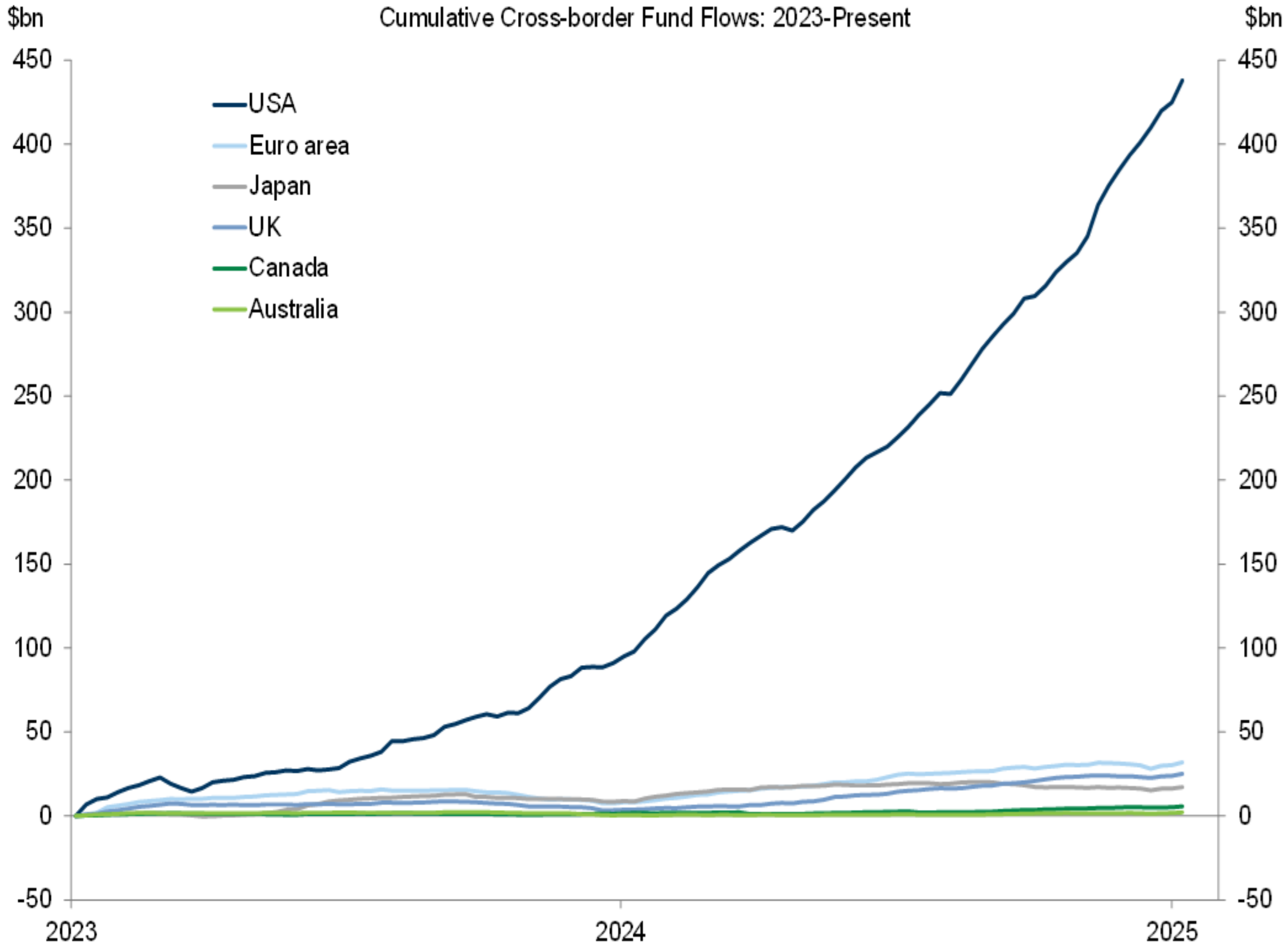
Both Foreign Direct Investments and portfolio flows have been Dollar supportive

Figure 4: Capital flows into the US have been comparatively heavy

1y rolling sum of FDI inflows in $bn

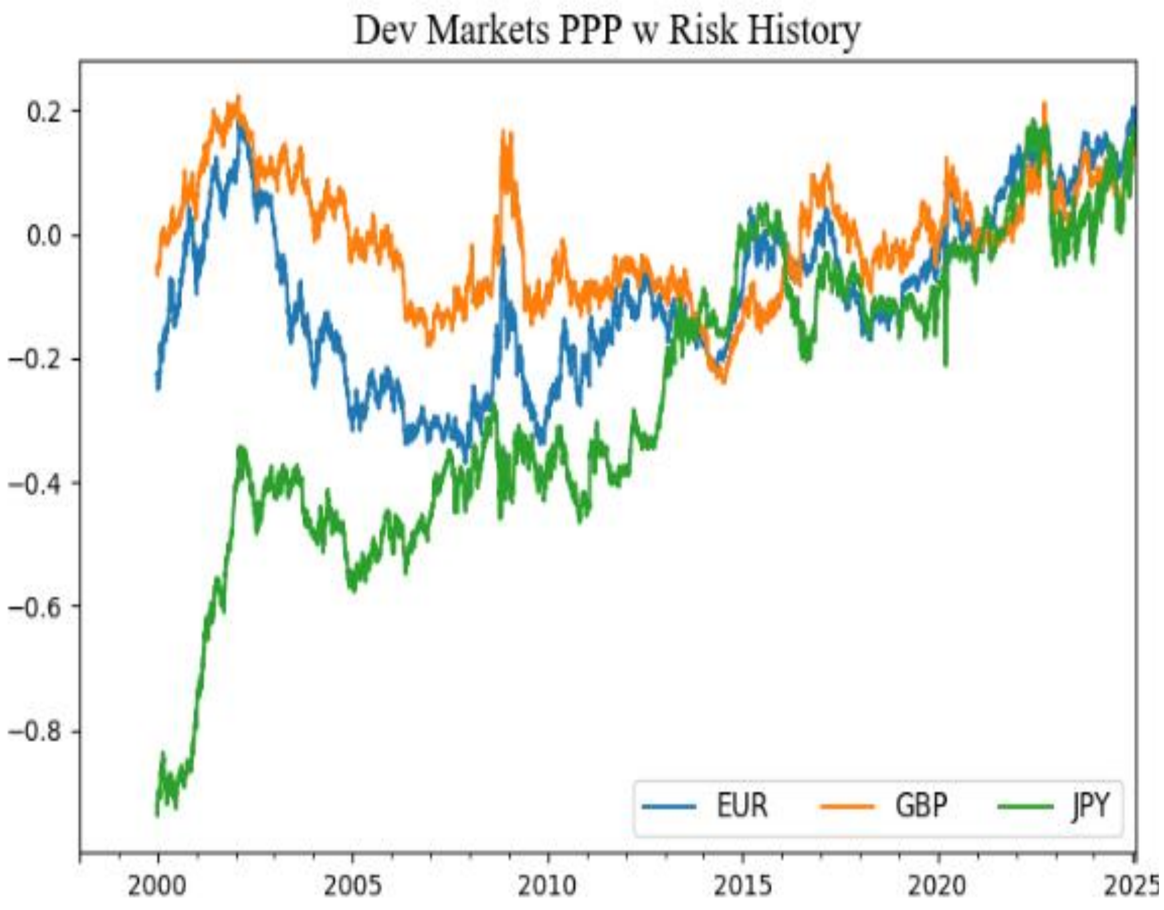


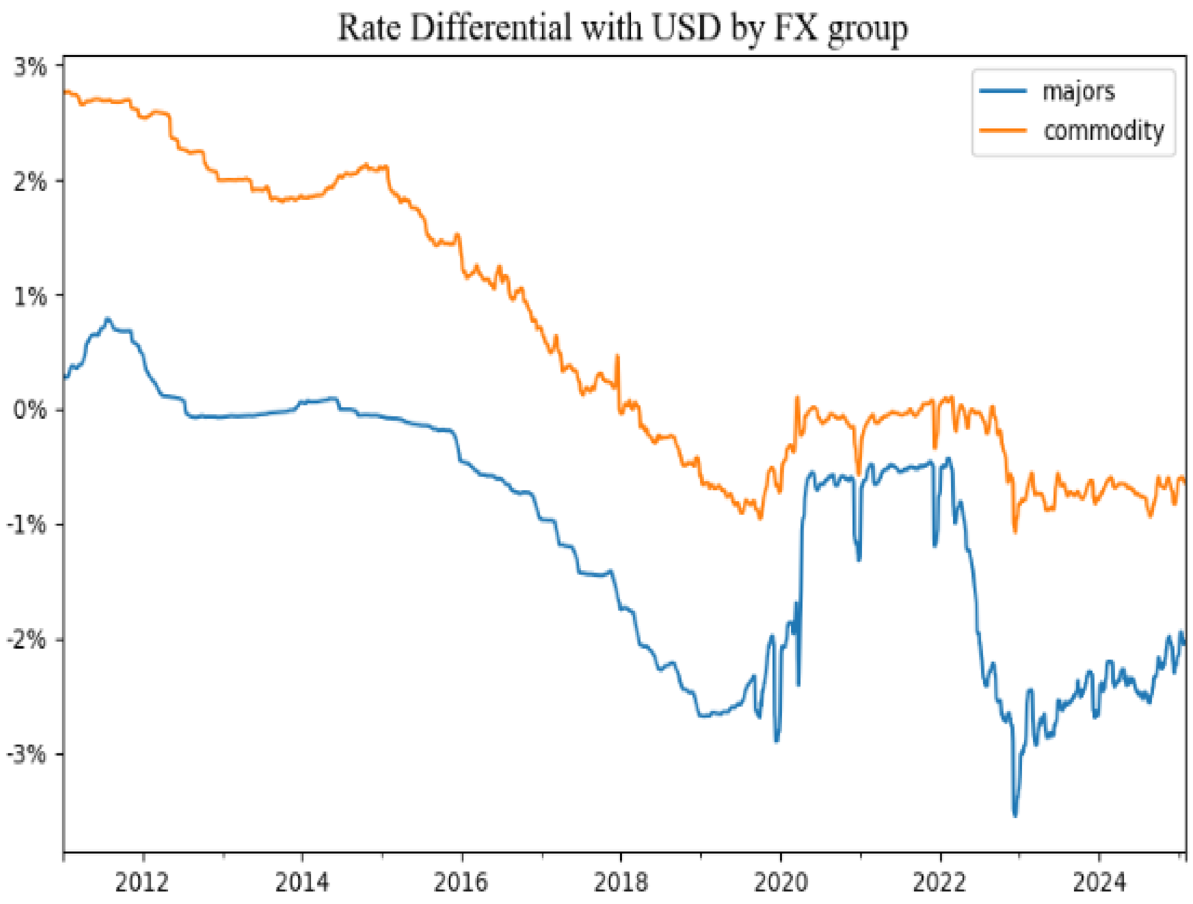
Source: OECD, Nomura



Major DMs' Valuation

- Dollar is expensive versus other DM currencies, though risk-adjusted valuation is less extreme
- Higher Carry offsets elevated USD valuation

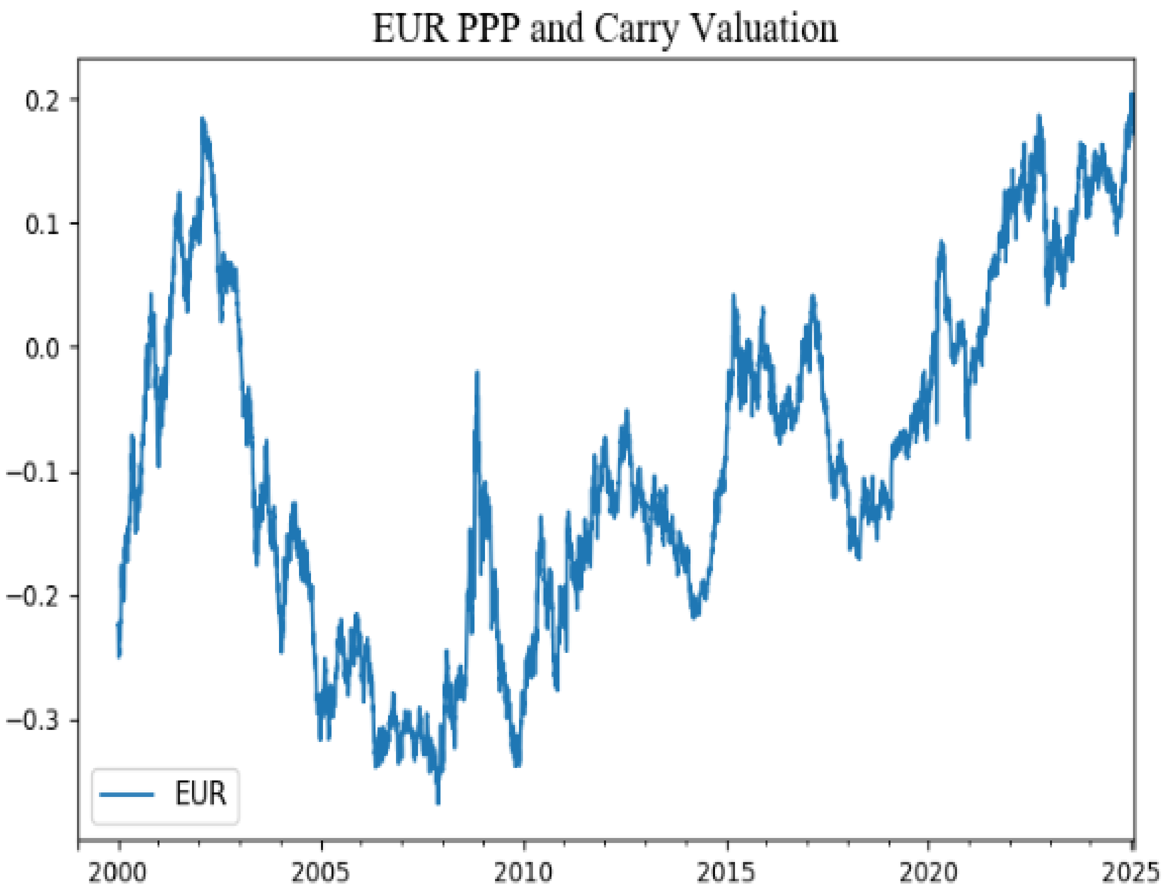


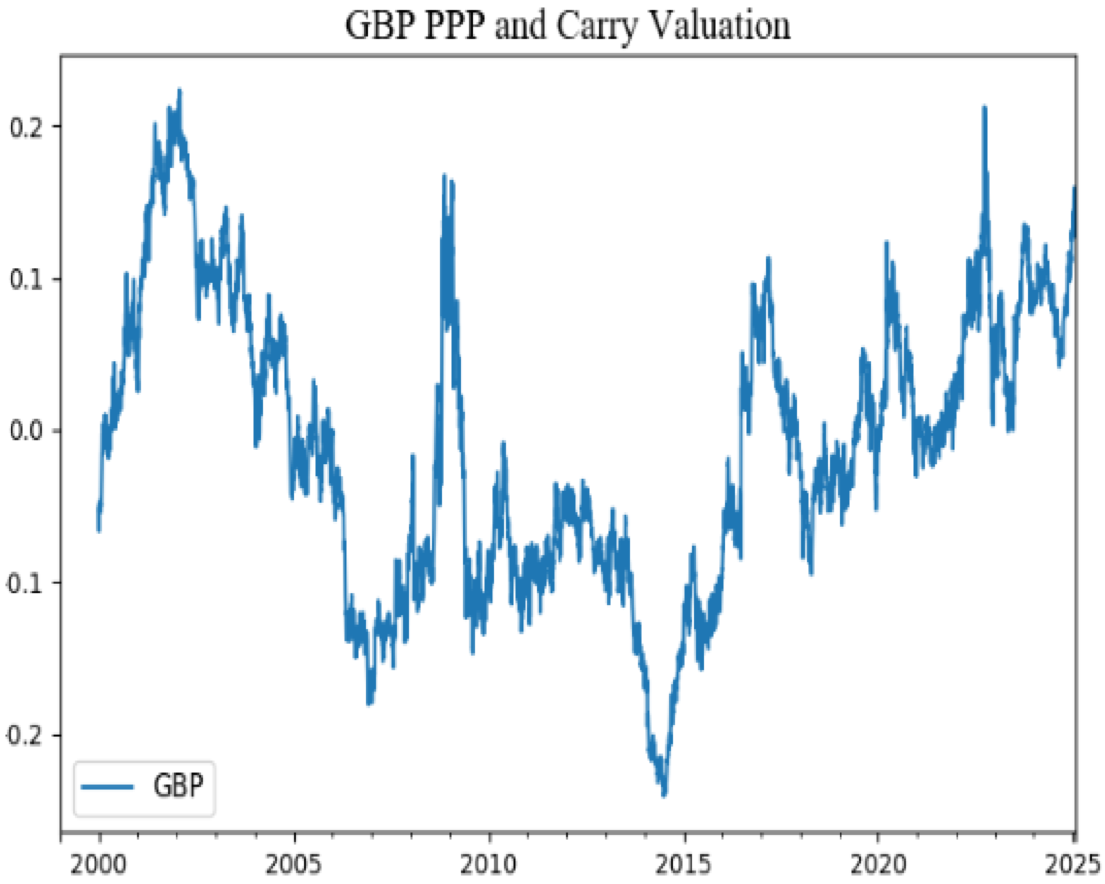


Source: Bloomberg, SECOR analytics

EUR and GBP

- Valuation for both EUR and GBP even after adjusting for carry
- But flows and policy divergence are USD supportive

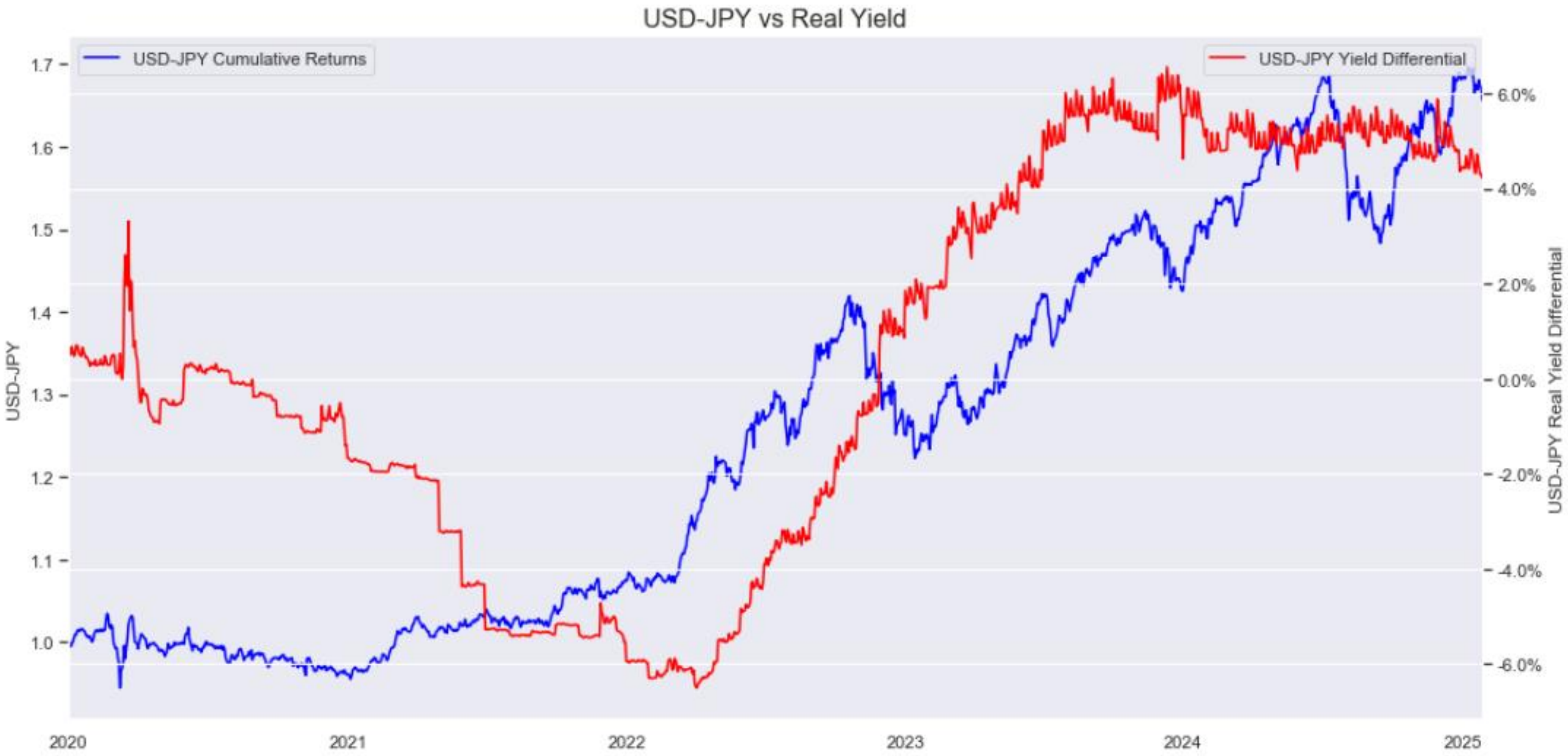




Source: Bloomberg, SECOR analytics

JPY – real yield is likely to remain the main driver

- Japan has negative real yield and Japanese Central Bank is hesitant to aggressively increase interest rates; this will likely continue to push JPY lower despite very attractive valuation



Source: Bloomberg, SECOR analytics

CNY remains exposed to many risks

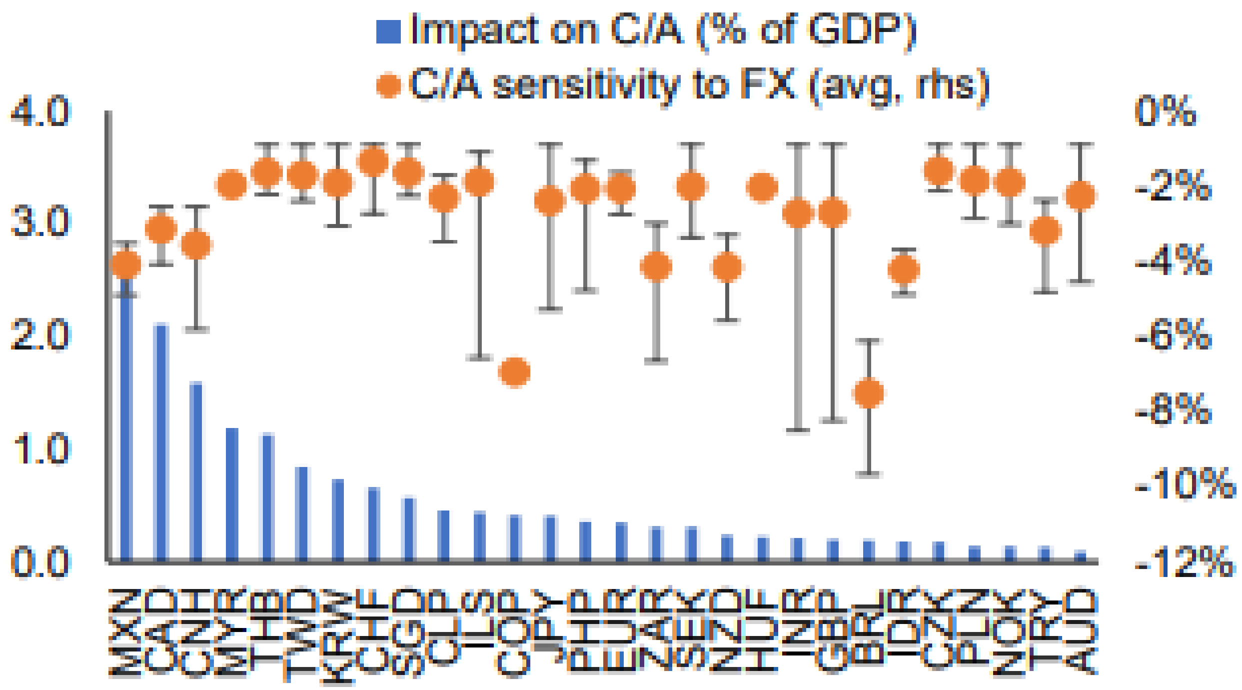
- CNY appreciated recently as Carry traders were reducing risks and as expectations of policy stimulus lifted China's equities
- Investors expect Chinese Renminbi to depreciate if Donald Trump gets elected
- Slowing China's economy and low interest rates provide additional impetus for the trade

Source: Bloomberg, SECOR analytics

Tariff Impact

- Mexico, Canada and China can suffer the most if the US applies tariffs
- The US represents close to 80% of Canada and Mexico total exports
- Direct impact on Europe from tariffs is smaller, but it may suffer indirectly from China’s slowdown and required increase in spending

Fig. 2: Tariff impacts on global current accounts



Notes: Tariff on China assumed at 60%, rest at 10%. C/A sensitivity is average of REER regressed on C/A and methodology from Cline.
Sources: Macrobond, Bloomberg, Cline, BNP Paribas

Conclusion/Summary

- USD continues to benefit from the “US exceptionalism” (strong growth and Tech sector)
- Investors expect elevated volatility due to tariffs and policy divergence

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Equity investments involve a high degree of risk. Equity securities may decline in value due to factors affecting securities markets generally, and equity securities generally have greater price volatility than debt securities/investments. Equity securities of certain jurisdictions may experience more rapid and extreme changes in value and may be affected by uncertainties such as international political developments, currency fluctuations and other developments in the laws and regulations of countries in which an investment may be made. There can be no assurance that return objectives will be realised and investors could lose up to the full amount of their invested capital. Fees and expenses may offset the trading profits.

Debt investments (such as, but not limited to, investment grade, high yield, emerging market debt, asset backed securities and insurance linked securities) involves special considerations and certain risks, including risk of default and price volatility, and such securities are regarded as being predominantly speculative as to the issuer's ability to make payments of principal and interest.

LDI and equity overlay strategies may invest and trade in many different market strategies and instruments (including securities, non-securities and derivatives) and may employ different investment, hedging, leverage and arbitrage methodologies, so the risks of those would be material to understanding the risks and benefits of the portfolio. Counterparty and ISDA arrangements may pose potential risk. Furthermore, derivative strategies may be exposed to the risk of market disruptions, volatility, and governmental interventions.

Illiquid investments (such as, but not limited to, private credit, private equity and infrastructure):

General/Loss of capital. Investment involves a high degree of risk. There can be no assurance that return objectives will be realised and investors could lose up to the full amount of their invested capital. Fees and expenses may offset the trading profits.

Limited liquidity. Investments in private markets may result in restricted liquidity since withdrawal rights are limited and interests are not freely transferable or redeemable. There is unlikely to be a secondary market for private market investments interests.

Volatility. Investment techniques used may include the use of leverage and derivative instruments such as futures, options and short sales, which could amplify the possibilities for both profits and losses and may increase volatility.

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Modelling Assumptions:

Forward looking return, volatility, and correlation assumptions have been derived by SECOR, and are based on a combination of: a) the historic performance of each asset class based on what we consider to be appropriate indices or suitable proxies, and over a period that we consider to be appropriate in light of prevailing market conditions (typically 10 years); and b) our judgement in relation to how historic performance, and its various components, may differ in the future. This may include, for example, ad-hoc adjustments to reflect our view that markets are over or under valued.

The resulting assumptions are assumed to be appropriate for asset and liability projections over the medium to long term i.e. 10 to 20 years or longer, and are net of all ongoing management costs and fees.

Expected returns for an asset class are generally built up from and include an allowance for our projected return on cash, inflation, spreads, risk premiums, liquidity premiums, potential losses, valuation adjustments, alpha for active management, management fees, other ongoing costs, and any other factors that we may consider are appropriate for the asset class and/or prevailing market conditions. Expected returns generally do not allow for SECOR advisor or fiduciary management fees, or any transition or rebalancing costs between asset classes or an existing portfolio.

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