EUROZONE UNDER SIEGE: CURRENCY TRENDS AND POLITICS

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"Oh, a storm is threat'ning
My very life today
If I don't get some shelter
Oh yeah, I'm gonna fade away.
War, children, it's just a shot away". "Gimme Shelter", The Rolling Stones

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OVERVIEW AND CONCLUSION

"America First!" and "Make America Great Again!" anthems inspire President Trump and many of his populist supporters. Many Americans of course have slogans, doctrines, and plans dramatically different from those of the President and his populist allies (and his establishment comrades). Despite America's sharp and wide-ranging partisan divisions, most Americans believe that America should be great (whatever that may mean in practice). They also agree that America's President and Congress (and other federal institutions), all else equal, should consider the country's needs first. Perhaps a majority of "We the People of the United States" retain faith that America in some fashion should be first (the leading nation) around the globe as well.

Nowadays Europe, like America, has a so-called establishment (various elites) battling fiercely against an array of populist adversaries. Yet the European establishment includes not only most leaders (and the bureaucracy) of the European Union and the Eurozone (and the European Central Bank), but also the political (economic) establishments of most of Europe's individual countries. So even though the European Union and Eurozone comprise various independent countries, and even though these nations contain diverse sets of right and left wing (and radical) political parties and economic ideologies, the overall European "establishment" ardently will promote "Europe First!" and "Eurozone First!" doctrines, particularly when the risks of European Union and (especially) Eurozone breakup appear rather high. Thus Europe/Eurozone preservation goals can trump narrower nationalist aims. Populist threats obviously are one source of such grave risks, which the United Kingdom's June 2016 Brexit "Leave" vote underscored. However, Europe's sovereign debt (banking; recall Greece and the European "periphery") crisis a few years ago reveals that other issues may motivate the European establishment to rally fiercely around a banner and fervently embrace policies to keep Europe unified.

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Napoleon: "In forming the plan of a campaign, it is requisite to foresee everything the enemy may do, and to be prepared with the necessary means to counteract it."

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The European establishments do not necessarily or always plan and act together. Yet despite their diversity, they are closing ranks, making statements and endorsing programs to ensure substantial European unity and their own places in power structures. On the national political front in several individual countries, this has included a shift to the right (particularly on the immigration issue). This mitigates some of the appeal of right wing (pro-nationalist; anti-globalist) populist candidates.

In the Eurozone context, a too frail Euro FX can reflect dangers to the Eurozone's integrity. America is a key European trading partner. The Trump camp forcefully proclaims its hostility to excessive weakness of the Euro FX and other currencies (such as the Chinese renminbi) relative to the dollar. The Trump regime (and many other Americans) probably would be pleased with a somewhat weaker dollar relative to its recent lofty high. So on the trade and currency landscape, some European mainstream leaders in response have suggested they want neither trade wars nor further Euro FX currency depreciation. Related to this, what does the ECB's March 2017 hint that it eventually will modify its current highly accommodative monetary policy indicate? It likewise probably signals a willingness to bolster the Euro FX.

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The Bank for International Settlements provides broad real effective exchange rates ("EER") for the Eurozone (Euro FX area) and numerous other nations. The current sideways pattern in the Euro FX broad real effective exchange rate ("EER") probably will persist for the short term. But as the 2017 European election calendar marches forward, the Euro FX EER probably will embark on a moderate bull trend. Major Euro FX EER support is well-entrenched and will not be broken by much, if at all. This Euro FX appreciation will occur not only on an EER basis, but also in the Euro FX cross rate relationship versus the US dollar. In general, determined efforts by the European establishment to retain power (defeat populists; avoid further European breakup) and bolster the Euro FX probably will succeed (at least for the next several months, and perhaps quite a bit longer).

EUROZONE: ECONOMIC COMMITMENTS, POLITICAL CALENDARS

Recall the European Central Bank President's "whatever it takes" 2012 statement (Global Investment Conference in London; 7/26/12): "When people talk about the fragility of the euro and the increasing fragility of the euro, and perhaps the crisis of the euro, very often non-euro member states or leaders, underestimate the amount of political capital that is being invested in the euro….we think the euro is irreversible….Within our mandate, the ECB is ready to do whatever it takes to preserve the euro. And believe me, it will be enough."

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The European Central Bank's highly accommodative policy, including its money printing regime, likely will remain intact for many months. However, its 3/9/17 meeting insinuated that a somewhat less accommodative policy eventually will emerge. This wordplay was a bullish sign for the Euro FX. The next scheduled European Central Bank monetary policy meetings are 4/27/17 (compare the timing of the two stages of the French Presidential election) and 6/8/17. Euro area annual HICP inflation attained the 2.0 percent signpost in February 2017.

Despite the explosive populist (nationalist) outcome and warning from UK's June 2016 Brexit "Leave" vote for Europe (and elsewhere), the allegiance of (especially) Germany and France to the European Union and Eurozone (Euro FX) probably was in June 2016, and still is, stronger than that of the UK to the EU. This year is the 60th anniversary of the 3/25/57 signing of the European Economic Community's founding Treaty of Rome.

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The European political situation obviously is fluid, with populist and other alternative parties having gained ground over the past few years. The UK Brexit outcome and Trump's US 2016 Presidential election victory surprised most political sentinels. So looking forward in regard to the European political landscape, clairvoyants should be cautious in making predictions. Nevertheless, in at least France and Germany, European establishment parties probably will defeat populist competitors.

Significantly, in Holland's March 2017 election, the Dutch prime minister's establishment party decisively defeated the challenge from the populist right wing, although the prime minister pushed some of its policies rightward to help accomplish this. He probably faces weeks of coalition building.

Some European swing voters fascinated by populist alternatives, after surveying the current American political theater in the wake of Trump's "populist" victory, arguably may move toward the establishment parties. The United States scene since Trump's January 2017 inauguration vividly portrays both American political divisions and the quality of America's current national leadership. Look at recent quarrels over immigration, health care, and the federal budget. Tax reform conflicts looms. Besides, suppose Congress enacts the tax and spending plans offered by Trump during his campaign. The budget deficit would grow substantially.

The NYTimes headlines: "Trump May Have Pushed Dutch Voters Away From Populism" (3/17/17, pA4).

Round one in the colorful French Presidential election fight occurs 4/23/17. A majority winner in the first round is very unlikely. The second round is scheduled for 5/7/17. Despite the advances and significant popularity of Le Pen's National Front, and though viewers should remember the lessons of Brexit and America's election, she probably will not win a majority vote in the second round. Recall that although Trump captured the Presidency via the Electoral College, he lost the American popular vote by slightly more than two percent. Majority vote, not an electoral college or a similar system, determines France's round two Presidential winner.

Germany's national election is 9/24/17. Although the current center-right and center-left parties closely contest the election, most pundits believe these establishment parties will not lose to populist (or extreme or radical) groups.

The Italian political scene is splintered, with the likelihood of potential populist outcomes unclear. Admittedly, the "Italian debate on merits of ditching euro grows louder" (Financial Times, 3/17/17). However, although Italy has a general election due within a year, that contest currently is not scheduled. Victories for mainstream parties in France and Germany will tend to assist European (and Euro FX) advocates within Italy.

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On Europe's economic disaster risk front, Greece has not escaped its debt debacle. However, perhaps inspired by talented soccer players, for several years European political and economic establishment generals have done an excellent job for of kicking the Greek economic problem down the road by means of assorted postponements and programs. In any case, these leaders (and their counterparts in many other leading nations and the IMF) probably will battle to stop the Greek situation from encouraging populist electoral gains.

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American captains who complain that the Euro FX is too low typically focus on the cross rate between the Euro FX and the US dollar. The dollar fell about 11.0 percent from 5/3/16's 1.162 to 1/3/17's low at 1.034 (26.1 percent from 5/8/14's 1.399 peak). However, the Euro FX has risen slightly against the dollar since January 2017, and that January 2017 bottom stands not much beneath 3/13/15's 1.046 low. On balance, the Euro FX cross against the dollar has moved sideways since around March 2015 (as has the broad real Euro FX effective exchange rate).

However, such foreign exchange (and trade policy) broadsides from the US Administration suggest that the US would applaud some strengthening in the Euro FX relative to the dollar.

EURO FX TRAVELS: EFFECTIVE EXCHANGE RATE

"The sword, the jewel, imagination
Cash, culture and violence
Violence, wealth and knowledge
Cash culture and violence
Oh you're riding and you're riding on the wings of destruction
Cash, culture and violence". The punk rock group Rancid's "Cash, Culture and Violence"

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The Bank for International Settlements provides broad real effective exchange rates ("EER"; CPI based; monthly average, 2010=100; data back to January 1994) for the Euro Area domain and many countries around the globe. The latest BIS release (3/16/17) gives statistics through February 2017 (next release 4/18/17).

The BIS effective exchange rate yardstick probably is superior to cross rates (such as the Euro FX against the US dollar) both as an indicator of Eurozone currency strength/weakness and regarding the extent of any economic and political crisis in the Eurozone (and European Union).

For the Euro FX EER's broad weight index (based on 2011-13 trade), the United States has a 13.2 percent weight. The US is an important trading partner for the Euro FX, but it is not the largest one. In the Euro FX EER, China possesses 17.9 percent. The United Kingdom's share is 9.9 percent. As for other significant portions within Europe, note Switzerland's 5.8pc and Poland's 5.0pc. The Czech Republic takes 4.1pc, Sweden 3.5pc. So the UK plus these four other European nations adds up to 28.3 percent. Japan has 5.2pc. Russia grabs 3.4pc.

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EURO FX BROAD REAL EER: ITS MOST RECENT MAJOR BEAR TREND

High	Low	All-Time High	All-Time Low
101.5; March 2014	86.9; April 2015	111.6; Apr 2008	83.4; Oct 2000
14.4pc decline			

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The broad real Euro FX EER established a major high in April 2008 at 111.6. The low during the October 2008 to April 2009 period was November 2008's 102.6. However, after ascending to 110.8 in October 2009 and attacking April 2008's ceiling, the EER retreated, making an important floor in June 2010 at 96.4. Although it charged uphill to April 2011's 101.7 height, this April elevation did not break over November 2008's depth.

Under assault during the European sovereign debt and currency crisis, the Euro FX EER crumbled after April 2011. The sustained bear move after April 2011 emphasized the fragility of the global, not just the European, economic recovery.

However, don't forget the European Central Bank President's "whatever it takes" statements defending the Euro currency and aiming to hold the Eurozone together. Alongside this resolute decree from the European Central Bank, the Euro FX EER established key lows around 91.9 in July and August 2012 (9.6 percent slide from April 2011's 101.7). The EER rallied up to March 2014's 101.5 peak, but subsequently suffered a bloody tumble to April 2015's 86.9 level, hanging above October 2000's record low.

The vicious Euro FX EER slump after March 2014 partly reflected the relative weakness of the European economy and the ECB's policy move involving greater easing on both the negative interest rate and quantitative easing (money printing) fronts. Contrast America's stronger economy and the Fed's tapering and ending of its beloved quantitative easing strategy in 2014 (the Fed announced the first round of tapering in December 2013; QE ceased October 2014).

For almost two years (since April 2015), the broad real Euro FX effective exchange rate has wandered sideways in a fairly narrow range. Its highs are September 2015's 92.2 and May 2016's 92.5 (UK's Brexit leave vote outcome 6/24/16). These heights only slightly pierced the critical 91.9 July/August 2012 barricade. The Euro FX EER average in October 2016 was 91.6. Following America's 11/8/16 election, it slipped, but only a modest 2.7 percent, to February 2017's 89.1; February 2017's level neighbors but nevertheless hovers above April 2015's low.

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Although marketplace history need not repeat itself, either entirely or even in part, it should not be neglected.

What are important near term resistance and support levels for the important broad real Euro FX EER benchmark?

Watch resistance at 92.5/91.2. Keep in mind the May 2016 and September 2015 tops; monitor summer 2012's major bottom at 91.9. A ten percent slide from March 2014's 101.5 top equals about 91.4. A five percent rally from April 2015's 86.9 is 91.2.

A ten percent rally from April 2015's 86.9 low is 95.6. A fifteen percent rally equals 99.9, close to the April 2011 (101.7)/March 2014 (101.5) elevation.

Key support resides at April 2015's 86.9 low. A fifteen pc drop from March 2014's plateau is about 86.2. The important February 2002 low was 88.0.

If the April 2015 floor is broken, remember October 2000's major low at 83.4. A 20pc break under March 2014's barrier gives 81.2. Arguably the Euro FX EER's major bear trend began not with its March 2014 height, but with April 2011's 101.7, or even April 2008's 111.6. A twenty-five percent crash from April 2008's top is 83.7 (the slump to April 2015's level was 22.1pc).

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Let's examine a few dates in the widely-watched Euro FX cross rate versus the US dollar in the context of this overview of the broad real Euro FX EER. As the wonderful Goldilocks Era of unending prosperity rolled to its stunning end, the Euro FX peaked at 1.6038 on 7/15/08. This was fairly close in time to the Euro FX EER's April 2008 pinnacle. The Euro FX's next major high against the dollar was 5/4/11's 1.4940. The noteworthy 2014 cross rate top for the Euro FX against the dollar was 5/8/14's 1.399, rather near in time to the Euro FX EER high in March 2014 at 101.5.

On balance, the Euro FX cross rate against the dollar, like that of the broad real Euro FX effective exchange rate, has paraded sideways since "around" late first quarter (March/April) calendar 2015.

The Euro FX low against the dollar was 3/13/15's 1.046 (not long before its April 2015 EER bottom at 86.9). The 12/3/15 low at 1.052 in the Euro FX was fairly close in price to 3/13/15's level. The Euro FX cross rate high in 2015 was 8/24/15's 1.171 (September 2015 EER minor top at 92.2). The Euro FX tops against the dollar were 5/3/16's 1.162 (remember the EER's May 2016 top at 92.5), 6/24/16's 1.143 (Brexit leave vote) and 11/9/16's (US election 11/8/16) 1.130. Though the Euro FX attained a new cross rate low beneath the 3/13/15 depth with 1/3/17's 1.034, that January level did not break March 2015's floor by much.

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The Euro FX's July/August 2012 bottom around 91.9 likely was branded as "too low"/"excessively low" by the ECB and its compatriots for the crisis situation around then. This opinion regarding that level probably continued for about a couple of years thereafter. However, everyone knows that economic and political situations can and do change. Thus the European establishment's summer 2012 viewpoint does not make that 91.9 level "excessively low" for policy guardians in subsequent times (such as from around late 2014 to the present).

So nowadays, a Euro FX EER level around 92.5/91.2 (and a bit less than that) probably is "low"/ "sufficiently low" from the perspective of the European Central Bank and other members of the European establishment. After all, a fairly (but not overly) weak Euro FX EER helps to achieve interconnected goals such as boosting GDP growth, reducing unemployment, creating sufficient inflation, and helping to hold the European Union (and the Eurozone) together. Won't progress toward such objectives help to subdue the dangers of populism (whether right or left wing)?

Nevertheless, the ECB, and indeed much of the European establishment community (and many other elites around the globe), probably do not want the Euro FX EER level to become "excessively low". That outcome arguably would warn of (confirm) grave dangers to European economic growth and Europe's political order.

An armada of intertwined variables of course influences currency levels and trends. What does the sideways movement in the Euro FX EER over the past several months suggest regarding the current opinion of much of the European economic and political establishment (and possibly similar establishment regiments elsewhere) regarding what is a "too low" level for the Euro FX EER? Around April 2015's 86.9 depth indeed may represent a "too low" level. October 2000's 83.4 bottom likely is "too low" and likely would be strongly defended by propaganda and action.

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The broad real Euro FX effective exchange rate created a noteworthy high in calendar first quarter 2014 (March 2014's 101.5). In calendar month terms, the tops of April 2008 (111.6) and April 2011 (101.7) are close in time to the March top. Not only was 2015's Euro FX EER low also in April (86.9). It also was about a one year diagonal bear move from March 2014, and thus a time to look for at least an interim trend change (the bear voyage is a longer duration diagonal downtrend if one selects as start dates the prior tops of April 2008 or April 2011). Thus an important (and double) bottom in the broad real Euro FX EER is fairly likely "around" calendar first quarter 2017. This second low already may be in place. If the Euro FX EER manages to fall under April 2015's low, it probably will not do so by much.

The trading history in the broad real trade-weighted US dollar intertwines with this perspective on the Euro FX EER. Several critical marketplace peaks in the broad real trade-weighted US dollar ("TWD"; Federal Reserve Board H.10 statistics; monthly average) have occurred during the first quarter of a calendar year. In addition to January 2016's important interim top at 100.9, recall the TWD's March 2009 major summit in at 96.7. Other major TWD pinnacles include March 1985's stratospheric and record 128.4, February 2002's towering 112.8, and January 1973's monumental 107.6. The high in the broad real TWD in its bull move from July 2011's 80.3 major trough is December 2016's 102.8 (January 2017 also about 102.8; February 2017 101.3).

In this timing context, note that an initial interim low in the Euro FX versus US dollar cross rate was 3/1/15's 1.046, and that so far the Euro FX remains above 1/3/17's 1.034 despite the Federal Reserve's raising of the Federal Funds rate and widespread anticipation that it will do so again in 2017.

The Euro FX EER's long bull move from October 2000 to April 2008 lasted about seven and one-half years. Suppose one chooses April 2008 as the commencement of the major bear move. The Euro FX depreciation from April 2008 to April 2015 is seven years; from April 2008 to approximately first quarter 2017 is nine years.

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For related marketplace analysis, see "Easing Comes, Easing Goes: US Government Interest Rates" (3/13/17), "Rhetoric and Global Currency Trends" (2/13/17), "Gold and Goldilocks: 2017 Marketplaces" (1/10/17), and other essays.

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