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# Currency Diversification : balance your risk and seize market opportunities

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## Investing in currencies – it's not about speculation:

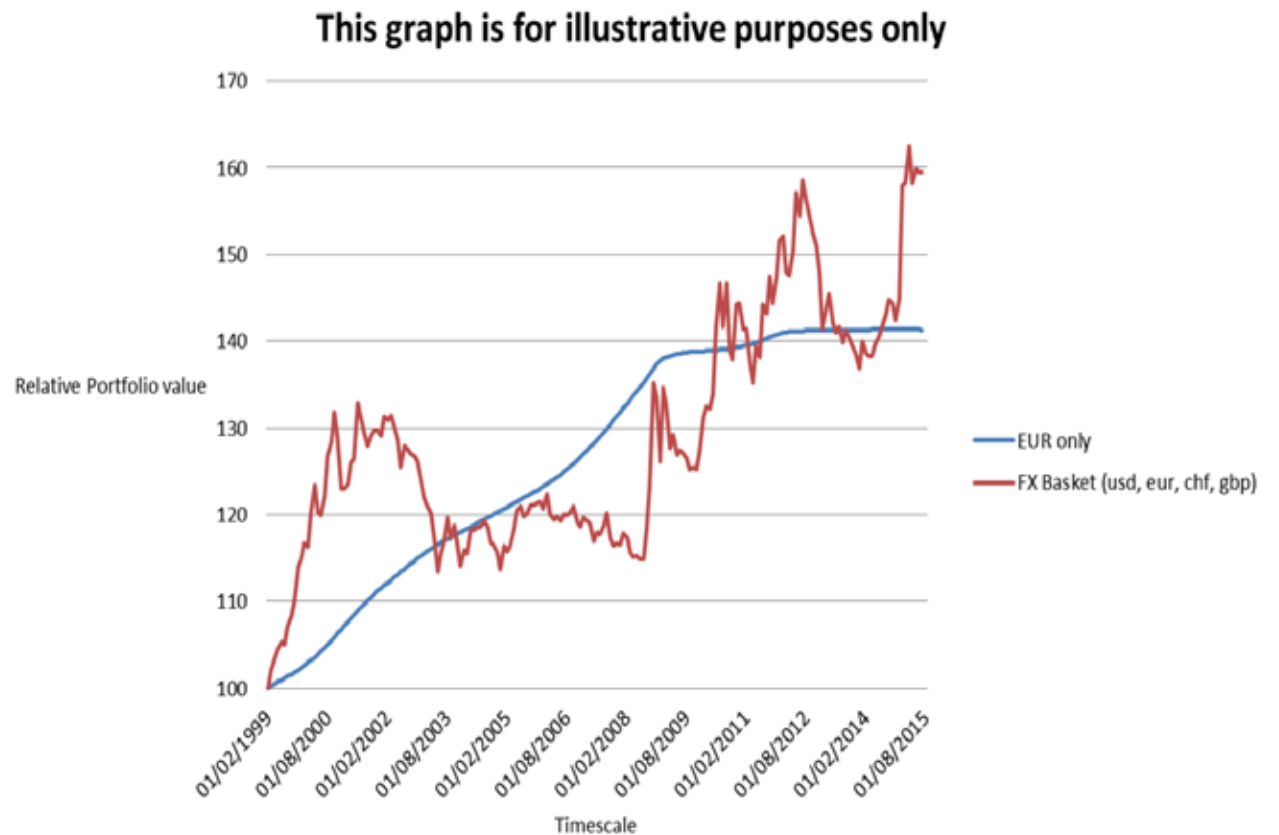
Due to the FX market's unique attributes, including its vast levels of liquidity and market inefficiencies arising from the varying activities of a huge range of market participants, investing in currencies could provide investors with the potential for profit.

For the investor not seeking to speculate but rather take steps to mitigate their exposure to the currency markets, there may still be diversification benefits given that currencies have tended to exhibit low correlations with other asset classes over time.

## Currency diversification – balancing your risk

To preserve one's wealth over time, investors should consider a long-term currency strategy. Keeping all of your eggs in one basket or currency, whether that is in US dollars or in Euros, may not be an ideal strategy from a long-term perspective. Yet many funds are dollar, euro, or yen denominated and the portfolio managers' main priority is to capture returns in the denominated currency.

Below is a graph of EUR denominated money market index vs equally weighted Currency Basket (USD, EUR, CHF, GBP) over the last 15 years illustrating the impact of currency diversification.



## Each currency has its unique characteristics

Some currencies tend to appreciate in times of financial market stress; others are sensitive to the global growth cycle and changes in commodity prices. Needless to say there is a large degree of variation among the behavior of different currencies but getting to know the general characteristics of the major currencies can better prepare investors to take advantage of investment opportunities

## Safe haven currencies

In times of heightened market volatility, investors tend to rebalance their portfolios toward assets that are expected to retain or even increase its value in times of market turbulence. A currency may be deemed to be of “safe haven” status if the country issuing it is itself “safe” and low-risk and possesses highly liquid financial markets. Ultimately, the ideal safe haven should be a place that is insulated from the global storm when the storm strikes. With this in mind, the usual safe haven candidates are the US dollar, the Japanese yen, and the Swiss franc.

## Commodity currencies

Currencies of commodity exporting nations such as the Australia, Canada, and Russia, are called commodity currencies. Naturally, there's a great degree of diversity amongst these nations in terms of trade balance, economic sophistication, etc. however because of the large currency inflows generated by proceeds of the sales of commodities, the value of these currencies is strongly correlated to the performance of the global commodity market.

## Interest rate advantage

As global monetary policy begins to normalise, countries that are likely to raise interest rates early, or have already been tightening should be well supported and remain relatively robust. On this basis, USD and GBP could benefit in the months ahead.

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