July 2016
Charts as of 07/05/16

The FRED Report – Currency Review

Welcome to our second Special Research Report on the currency ETFs. The last report we did on these was in 2012 and another is appropriate now for two reasons: First, it looks to us as if the relationship between the dollar and commodities is changing, and second it looks as if we could be entering a period of dollar strength.

In our first report, back in 2012, we looked for a rally in the European currencies, and this occurred, with an advance into 2014 or so. The dollar then gained strength in 2015, and is now in a consolidation. It has become oversold within that consolidation and started to rally toward the top end of the range and might break out to the upside.

The "commodity economy" currencies we follow, FXA and FXC are in interesting positions. FXC is building a Head and Shoulders bottom and could break out to the upside, while Australia looks less strong. This suggests continued strength in the US vs. Asia.

In the Asian currencies, Japan has been strong of late, rallying into resistance in the 95 to 97-area. The Chinese currency is weak, but so far holding support, and the Singapore Dollar is showing some bottoming signs after a multi-year downtrend.

Region | ETF Currency	Page
North America	
US Dollar (DXY and UUP)	2-3
CurrencyShares Canadian Dollar Trust (FXC)	4
Asia	
CurrencyShares Australian Dollar Trust (FXA)	5
CurrencyShares Chinese Renminbi Trust (FXCH)	6
CurrencyShares Japanese Yen Trust (FXY)	7
CurrencyShares Singapore Dollar Trust (FXSG)	8
Europe	
CurrencyShares Euro Trust (FXE)	9
CurrencyShares British Pound Sterling Trust (FXB)	10
CurrencyShares Swedish Krona Trust (FXS)	11
CurrencyShares Swiss Franc Trust (FXF)	12
Hedged ETFs	
WisdomTree Europe Hedged Equity Fund (HEDJ)	13
PowerShares Europe Currency Hedged Low Vol (FXEU)	14
MSCI Emerging Markets Hedged Equity ETF (DBEM)	15
MSCI EAFE Hedged Equity ETF (DBEF)	16
WisdomTree Japan Hedged Equity Fund (DXJ)	17
PowerShares Japan Currency Hedged Low Vol (FXJP)	18
MSCI Japan Hedged Equity ETF (DBJP)	19
Disclaimer	20

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North America ETF Currency: US Dollar Index (DXY)

The Dollar Index is moving toward the top end of the trading range, as drawn: The Dollar Index looks to have completed an intermediate-term bottom in 2014. Sentiment on the dollar has become more bullish, but is still not elevated enough to be concerned. DXY should advance to test the top end of the range, and may do more. Note that over the last few weeks we have seen changes in the relationship between the dollar and commodities, and we believe these should continue – a strong dollar and strong gold, for example, could continue for a while.

North America ETF Currency: PowerShares DB USD Index (UUP)

UUP has started to trade up toward the top end of the range: The UUP has held support at 24, and should test 26. However, note that this chart has underperformed the actual cash dollar index substantially (see previous page). Still, UUP is the best way to trade an advance in the dollar, at least in the ETF world. Our first objective for the intermediate rally has been 25, and this has been achieved. Some pullback could occur over the next few months to resolve the short-term overbought condition, but ultimately we expect 26 or higher to be tested. See the previous page for more info on the changes in relationships with commodities, and such, that look possible.

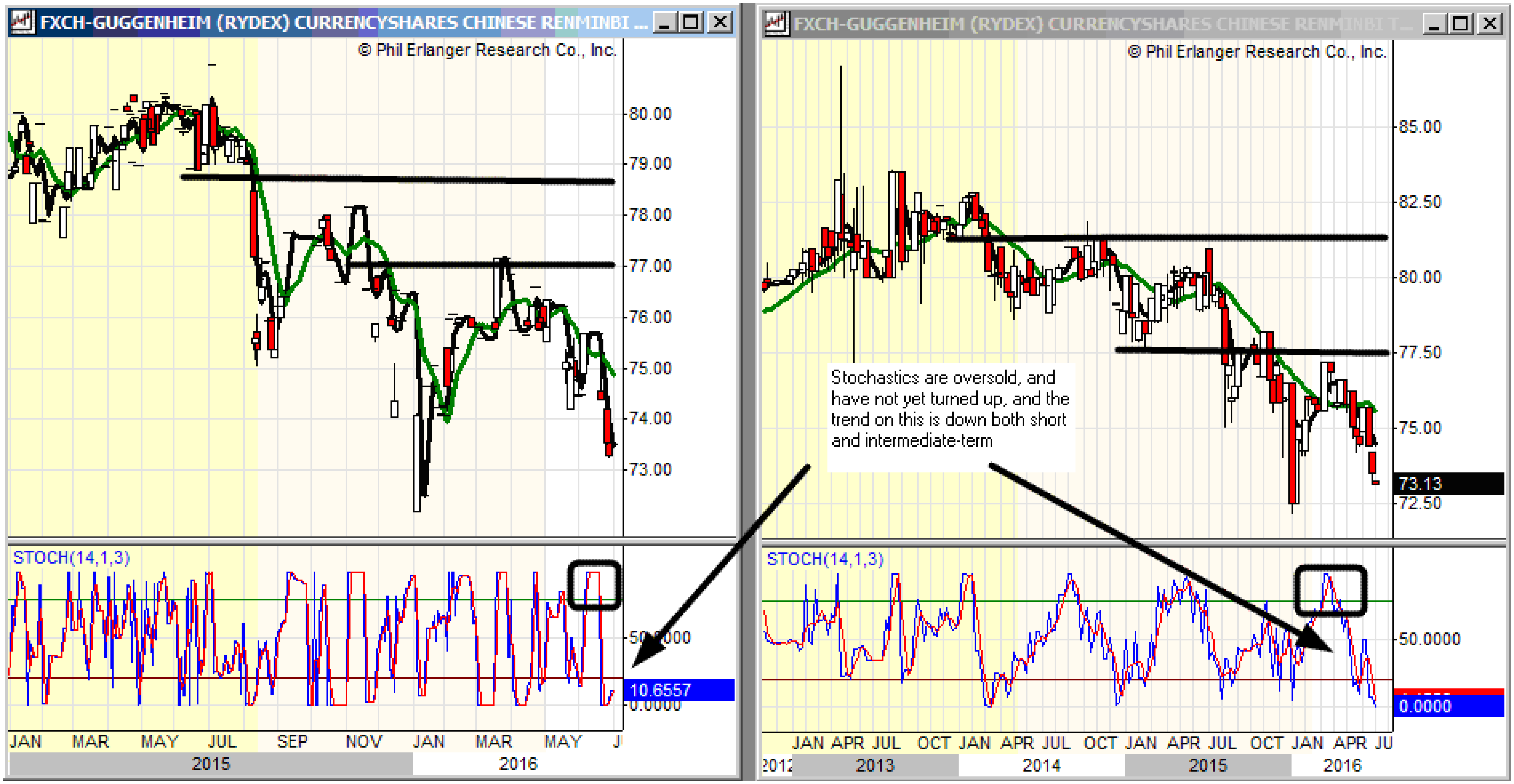
North America ETF Currency: CurrencyShares Canadian Dollar Trust (FXC)

The Canadian dollar is forming a Head and Shoulders bottom, as drawn: Canada, as well as Australia, is part of a potential resurgence in commodity prices. FXC may be ending a multi-year downtrend through the formation of a Head and Shoulders bottom. This would be confirmed by a move above 80. FXC has been performing better than FXA since 2015. We note this as this relationship can be a proxy for the performance of the US vs. China. FXC is a commodity oriented currency that is tied more to the US, while FXA is tied mostly to the Asian economies. The next weekly stochastic buy signal should be a strong indication to buy EWC, Canadian equities, as well.

Asia ETF Currency: CurrencyShares Australian Dollar Trust (FXA)

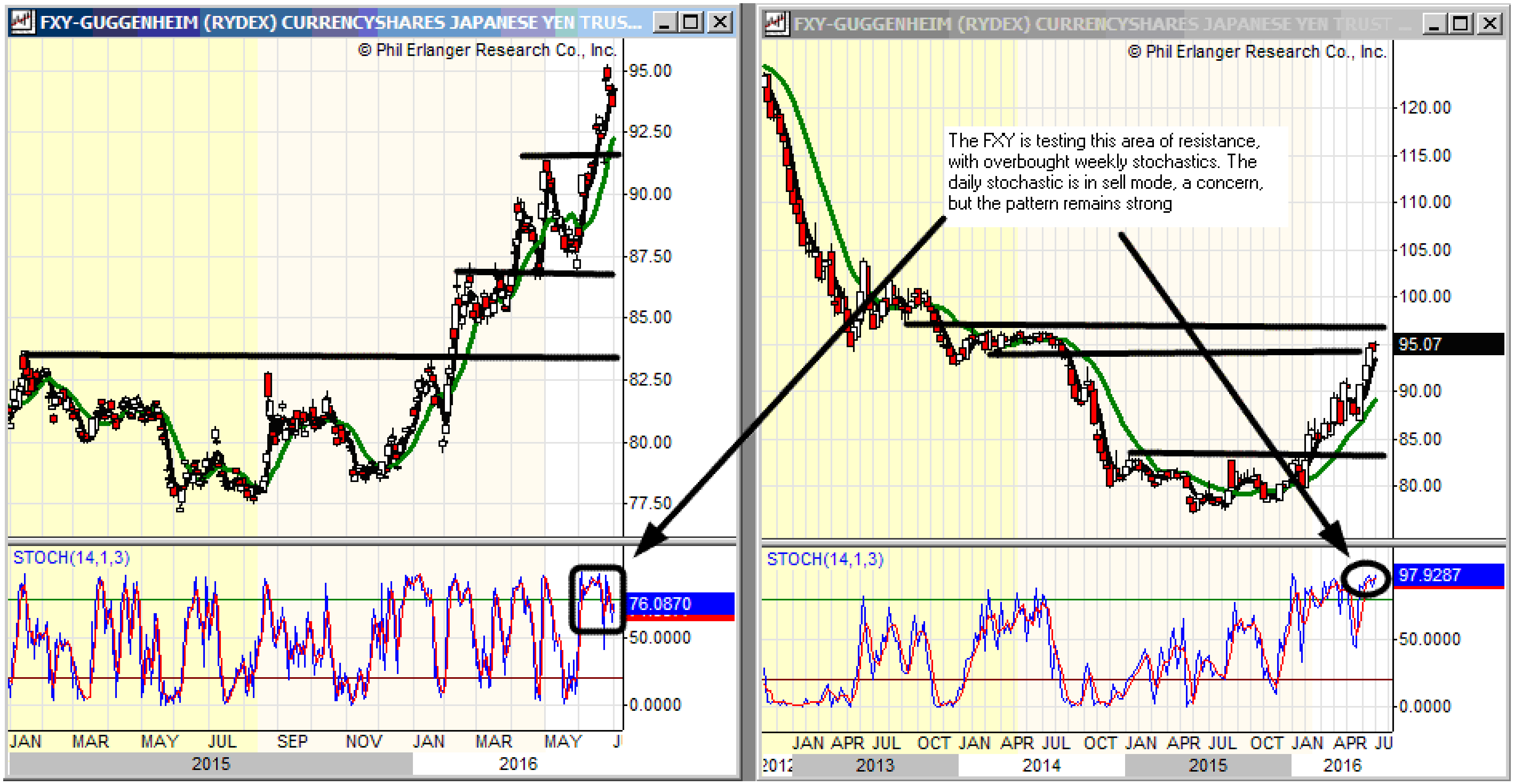
The Australian Dollar has a similar, but weaker, pattern than FXC: The daily and weekly stochastic are both giving buy signals, and the chart is a bottoming pattern. The FXA is a double bottom and the first retracement after a rally has made higher lows, at least so far. For this market to look really strong, it should penetrate 80 on the next rally, which may have started. As mentioned, we prefer FXC as it is an upward sloping Head and Shoulders pattern with a higher right shoulder, while this has a lower right shoulder. We think this reflects the weaker fundamentals of Asia as opposed to North America.

Asia ETF Currency: CurrencyShares Chinese Renminbi Trust (FXCH)



<u>The Chinese currency chart is in a pronounced down trend:</u> There has been so much recent turmoil in Europe that this chart, which is close to exceeding the January low, is not being noticed. The formation suggests that new lows will be seen by the end of 2016. This is a concern as turbulence in the Renminbi lead to a Chinese equity decline that hurt US stocks in January. Unless this trades above 77 we will monitor this carefully. Also, watch DSUM carefully as that bond ETF can sometime show which way the Chinese currency will go.

<u>Asia ETF Currency</u>: CurrencyShares Japanese Yen Trust (FXY)

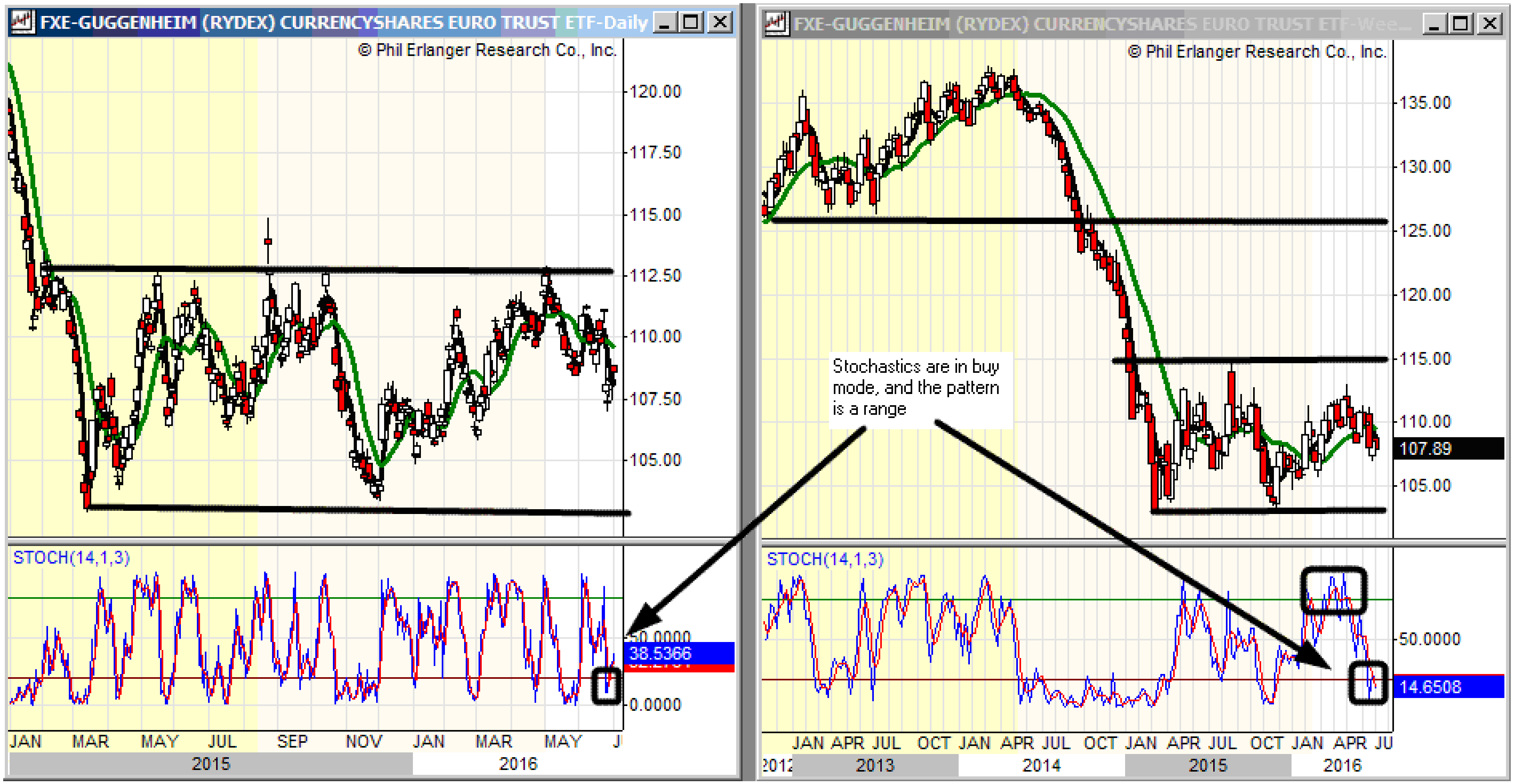


<u>The Japanese Yen is testing resistance after moving out of a bottoming formation:</u> The FXY has stronger than the Euro as we have forecast, but this may finally be ending as it is now in resistance. This action, especially over the last few months, has hurt the hedged ETFs relative to their un-hedged brethren. We also note that the dollar has gained strength along with this, something else we forecast was possible and which has surprised many. This is the best example of why we remind advisors that the dollar is a BASKET, and not an individual currency. FXY may now be at enough resistance that the hedged units should start to work again. We will watch this carefully.

Asia ETF Currency: CurrencyShares Singapore Dollar Trust (FXSG)

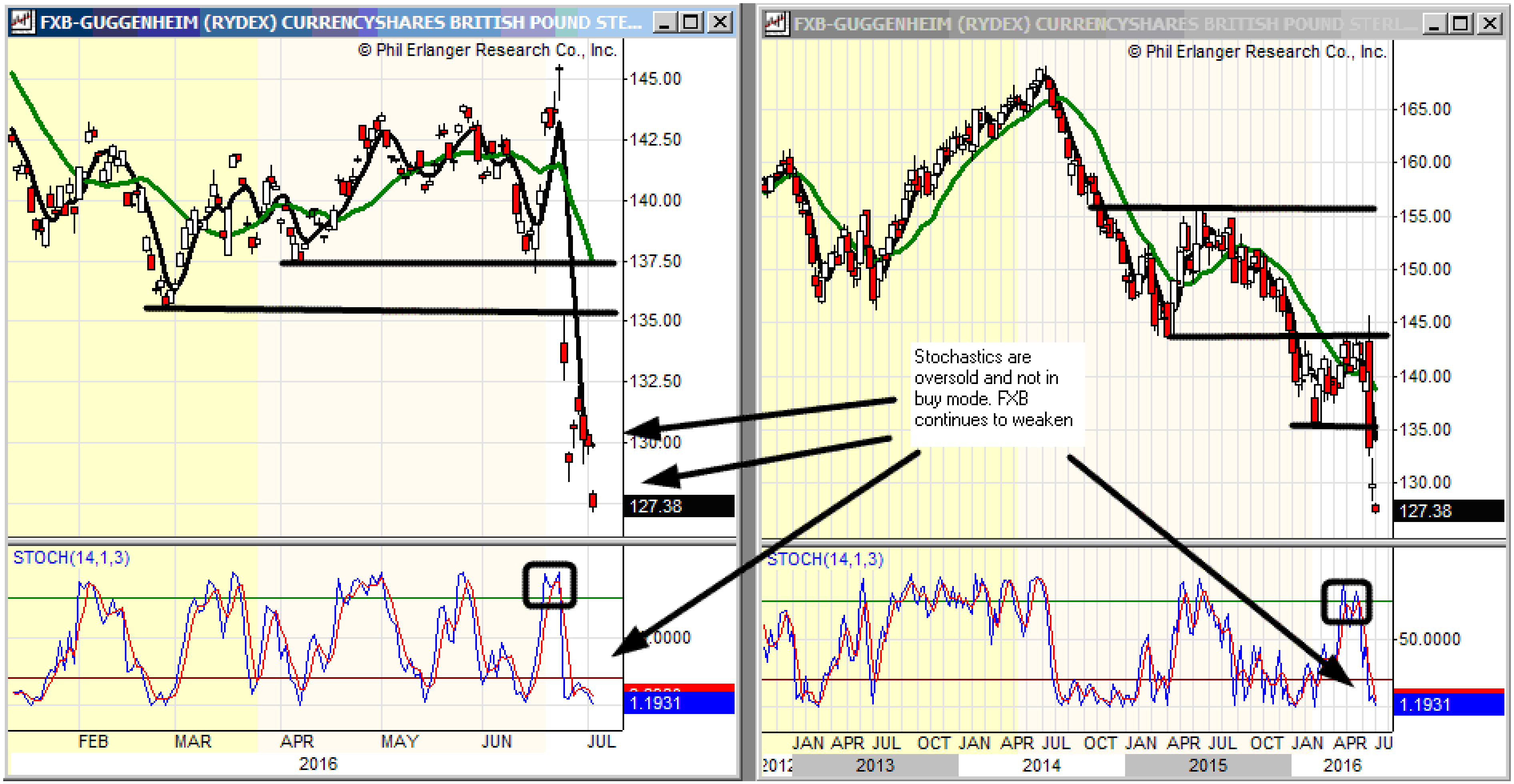
<u>The Singapore Dollar is also making a Head and Shoulders bottom:</u> This currency looks similar to FXA, and is in a bottoming pattern that would be confirmed on a move above 75. This is a fairly new ETF, and Singapore has been overlooked over the last year. But, there are enough bottoming signs such that strength in this might lead to strength in EWS, which also has a Head and Shoulders bottoming pattern. Below 67 would be detrimental and a sale should this occur.

Europe ETF Currency: CurrencyShares Euro Trust (FXE)



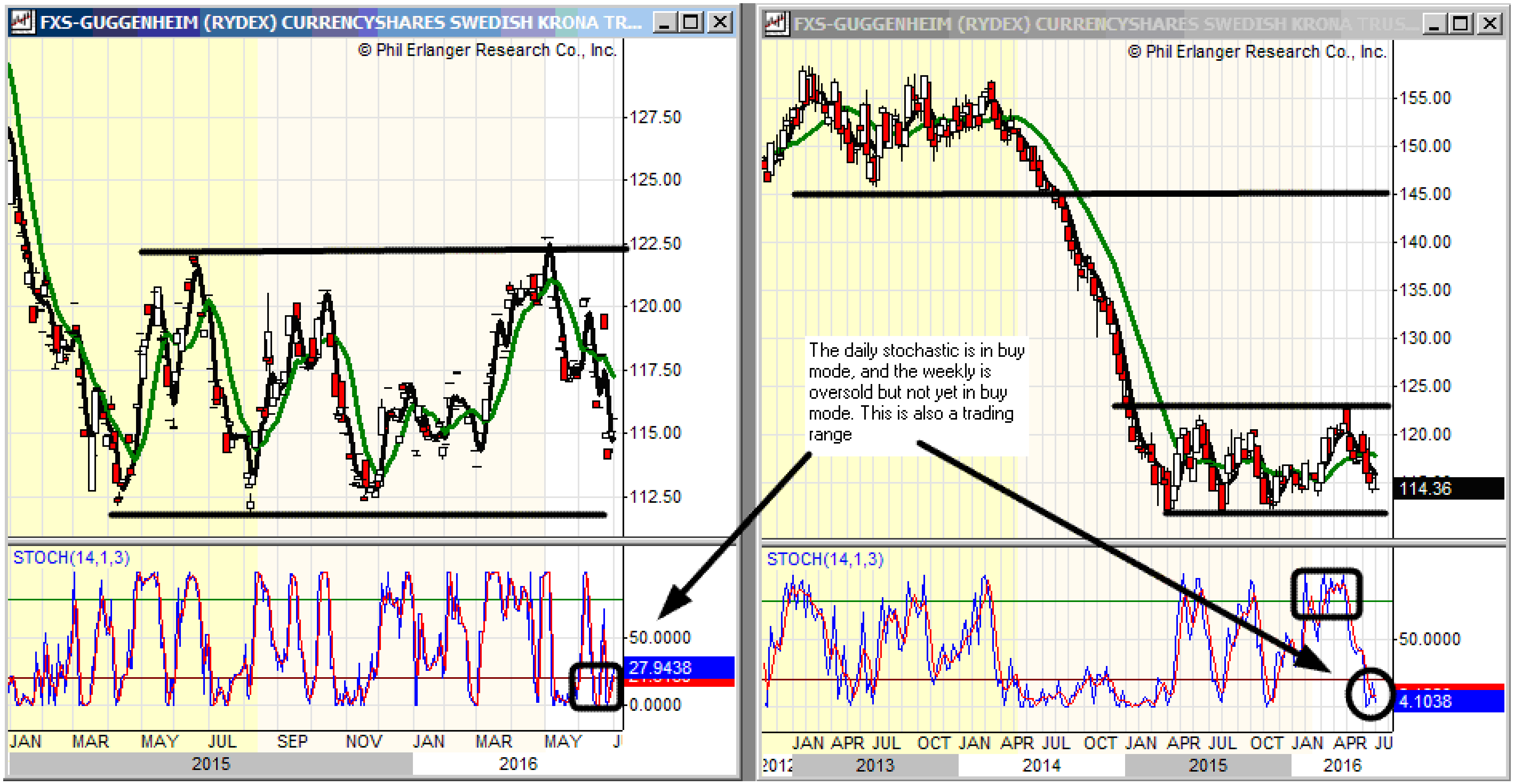
<u>The Euro has weakened since the start of 2014:</u> The FXE has weakened sharply over the last two years, breaking short-term support at 125, and making a choppy bottom in 2015 to present. The daily and weekly stochastics are in buy mode, suggesting a rally is possible from this area, but obviously this is a "newsy" market that may not do much but consolidate for a while. Remember, though, that currency markets can trend more than other markets – a concern indicating that this end up being a continuation pattern to the downside if 102 breaks.

Europe ETF Currency: CurrencyShares British Pound (FXB)



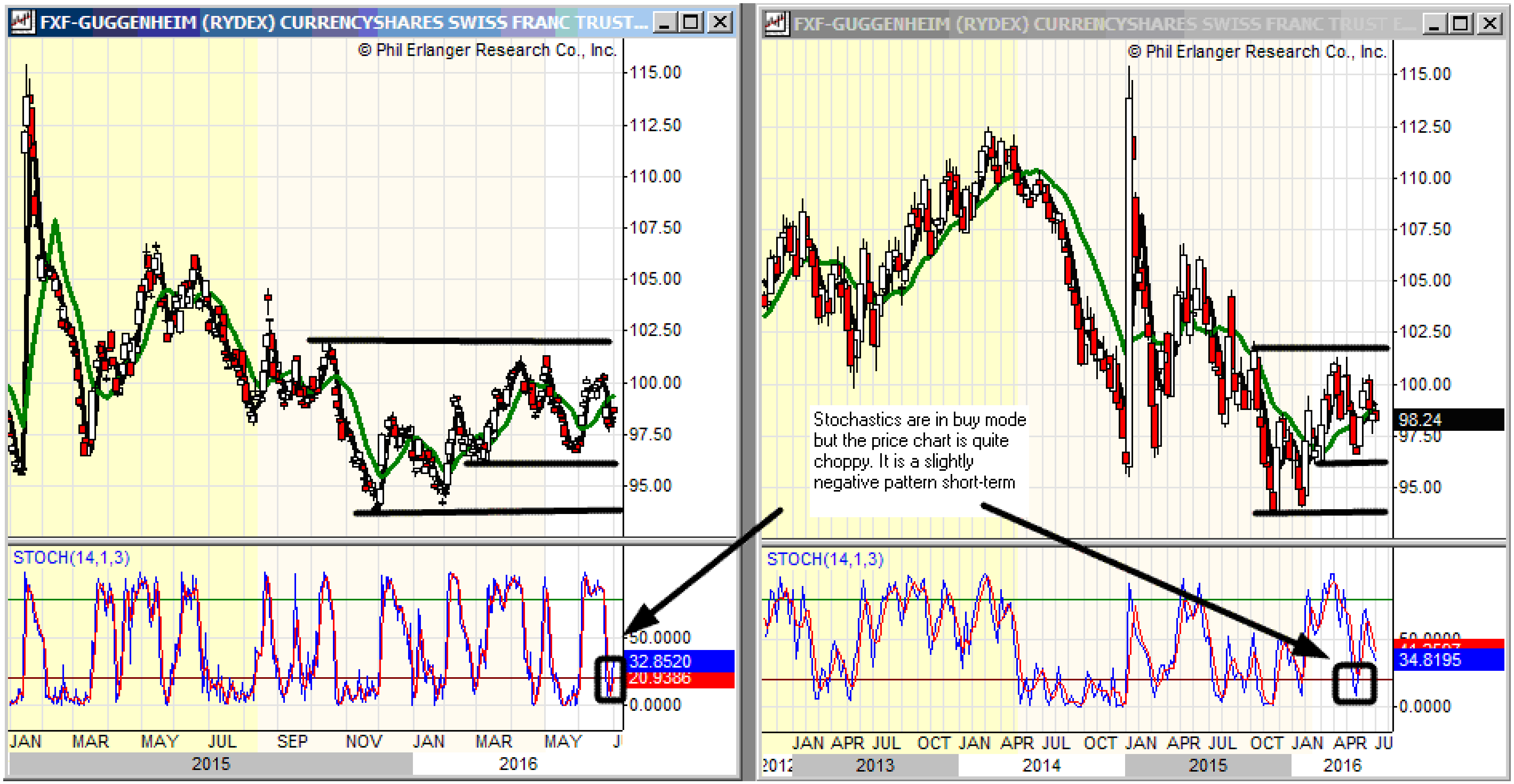
<u>FXB has continued to weaken:</u> The chart is weakening on Brexit news, and the question most have is where to try and buy this currency. There is support from the 1980's at 124 – 125 (not shown on this chart), and the real answer is to wait for a reversal. Back above 130 would be the start of a reversal and above 136 would tend to confirm this is underway.

Europe ETF Currency: CurrencyShares Swedish Krona Trust (FXS)



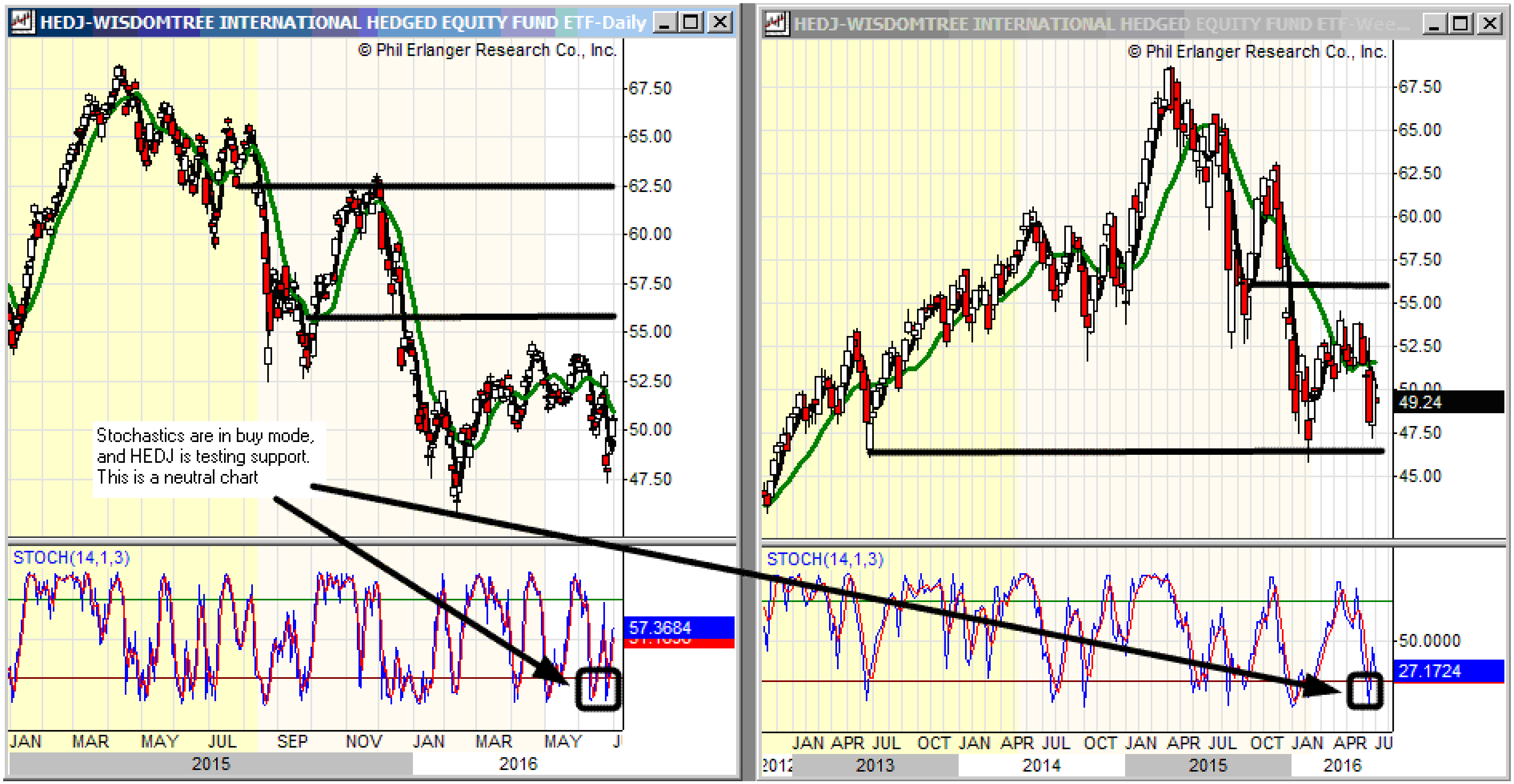
The Swedish Krona is also a trading range: Sweden has been one of our favorite European equity markets for some time. This chart is now weaker than FXE, but not by much. FXS remains in a trading range. If this moves above the 125 area intermediate resistance it would be on the road to recovery – for now it is a neutral pattern. Like FXE, it is possible that this is a continuation pattern to the downside – below 111 would confirm that this is so.

<u>Europe ETF Currency</u>: CurrencyShares Swiss Franc Trust (FXF)



<u>The Swiss Franc is our favorite European currency, and could rally from this area:</u> The Swiss is our favorite European currency. The big spike up in 2014 is when it decoupled from the Euro, but it has gone back to trading in line, more or less, with FXE. The intermediate stochastic is positive, and the daily has just given buy indications. While this has been officially "decoupled" from the Euro, in fact the two currencies will tend to trade together unless there is sufficient stress in the Euro, in which case it normally outperforms. As such this makes it a good hedge for European problems.

Hedged ETFs: WisdomTree Europe Hedged Equity Fund (HEDJ)

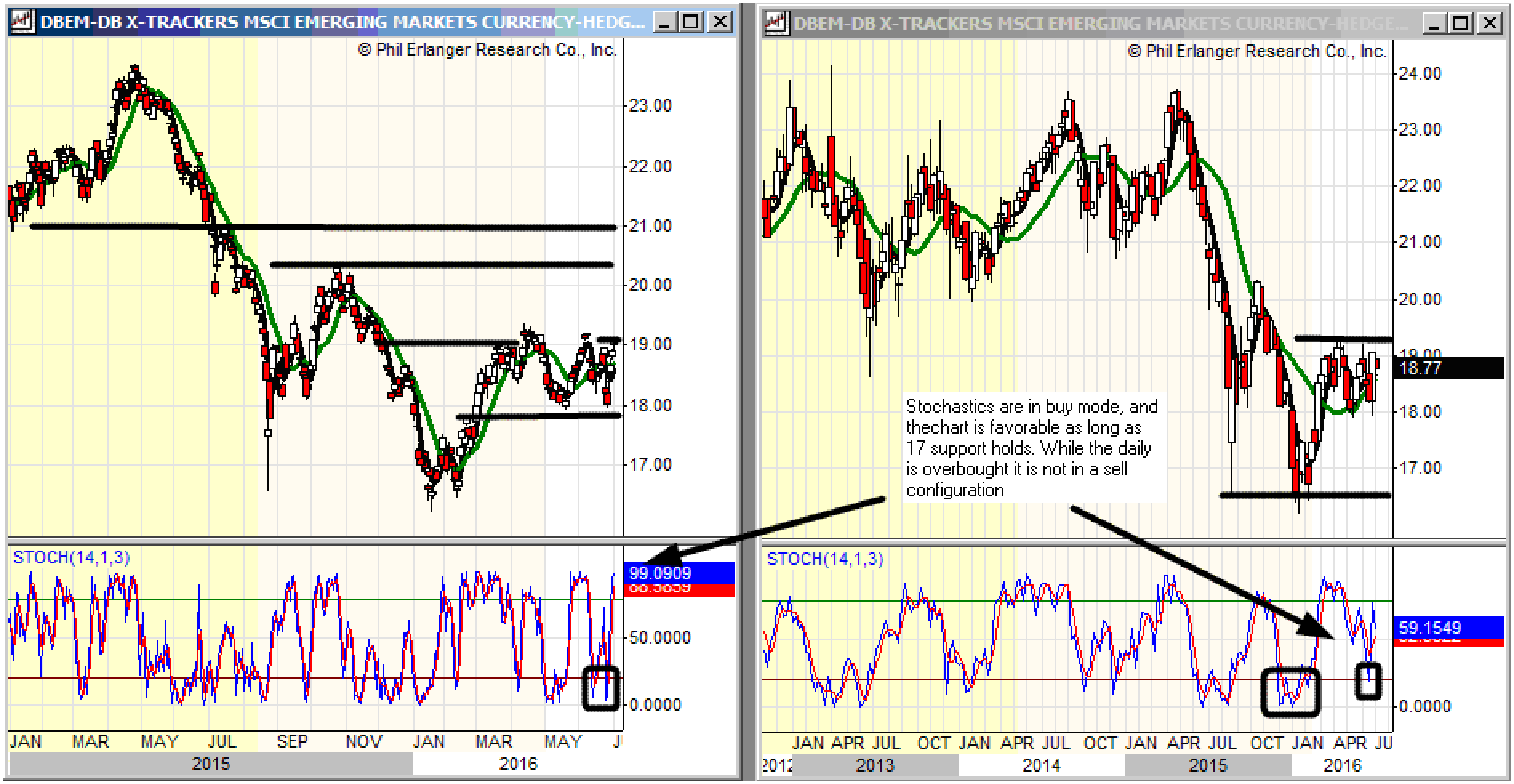


HEDJ is testing support in the 47-area: HEDJ has held up throughout the recent European turmoil, and is a satisfactory chart if you need to have European exposure. We have not been recommending Europe for some time as the overall pattern of most of their markets is negative. Indeed, what we have seen and written about is that the weak countries have gotten weaker, and the strong have improved, since 2009. Below 45 would imply a new down-leg in this chart, and more problems in Europe. We have recommended EWL (not shown) as a way to invest in Europe if you must.

Hedged ETFs: PowerShares Europe Currency Hedged Low Vol (FXEU)

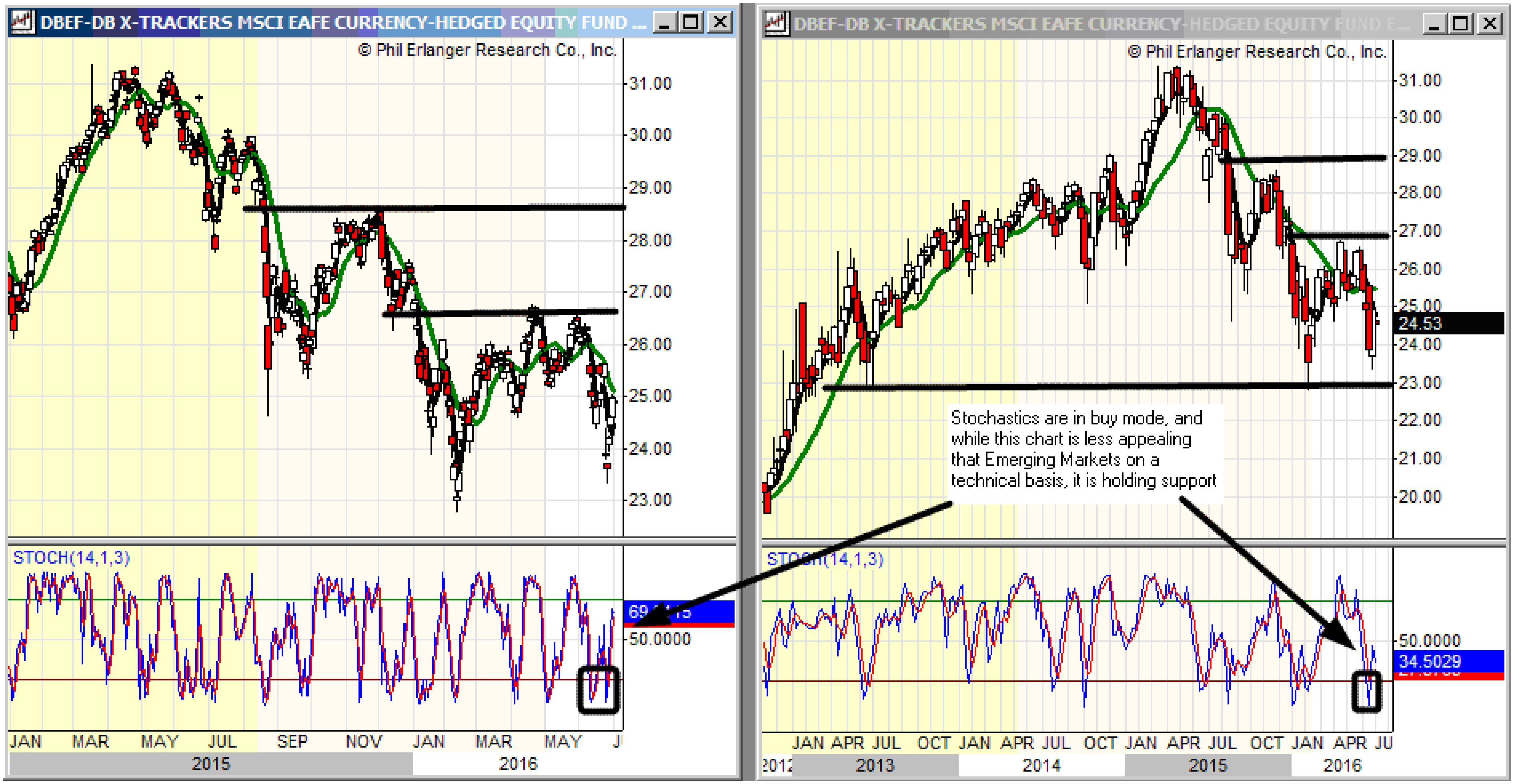
FXEU is a new ETF, and the chart is somewhat unreliable: The pattern is decent and the low volatility process has worked in other markets. We like the idea of this especially as Europe is likely to have more turmoil. Also, the dollar looks to rise intermediate-term and this should do well in that environment.

Hedged ETFs: MSCI Emerging Markets Hedged Equity ETF (DBEM)



<u>Emerging Markets are our favorite part of international, and hedging the currency has not impacted the chart:</u> We have been using a combination of Emerging Market equities and bonds to gain exposure to this area of the market. Given the turmoil in Europe this has been our favorite area for those advisor who must have international exposure. There are all sorts of bottoming signs in this chart as long as the support in the 17-area holds, and above 19, then 21 would suggest a new uptrend.

Hedged ETFs: MSCI EAFE Hedged Equity ETF (DBEF)



EAFE looks less appealing than Emerging Markets at this juncture: We continue to view the developed part of "International" as less appealing that Emerging Markets, but as long as this holds the 23-area support it is buyable. Above 27 would be strong, and we would watch for this to add to positions. For now this is a "hold" for us.

Hedged ETFs: WisdomTree Japan Hedged Equity Fund (DXJ)

<u>DXJ has started to weaken, in large part due to recent Yen strength:</u> We removed DXJ from our models a few months ago. At that time, we advised trading SCJ, which has done well. Now, this is starting to weaken and unless back above 40 soon there could be more weakness. See the chart of FXY, also in this Report. If that moves above 96 this should test 30 or so. Caution is indicated.

Hedged ETFs: PowerShares Japan Currency Hedged Low Vol (FXJP)

<u>Very limited history makes stochastic analysis difficult to employ:</u> But, given the strength in the FXY we would consider adding this for Japanese exposure, especially for cautious money. We have been recommending SCJ, and that has done well but could quickly reverse. This might be a good solution.

Hedged ETFs: MSCI Japan Hedged Equity ETF (DBJP)

DBJP is a stronger chart than DJX, and is almost in buy mode: This ETF is doing a better job of holding the lows than DJX, and the stochastic pattern is stronger. Those who have a tax loss in DJX that can sell that and buy DBJP should consider this, especially if FXY starts trading below 92. Japan is not a favorite market relative to Emerging Markets (we like some stocks such as HMC and SNY), but if you want a Japan position and are already in SCJ this is a good addition.

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