



Investment Views

FEBRUARY 2026

Deciphering the US Dollar's Strategic Descent

One of the topics du jour in the opening months of 2026 has been the structural softening of the US dollar. Having recently touched a four-year low on a trade-weighted basis, the greenback's retreat is not merely a market correction but a deliberate feature of contemporary American economic policy. For the sophisticated investor, understanding the drivers of this "weaker dollar" regime is essential to successfully navigating the shifting investment landscape.

While a strong dollar traditionally signals national economic vigour, it can simultaneously act as a "gold-plated anchor" on domestic growth. The current administration's preference for a depreciated currency is a pragmatic pivot aligned with its "America First" industrial strategy. What do we mean by that?

First, a weaker dollar acts as a global discount code for American-made goods. When the dollar falls, the cost of a Boeing 777 or a shipment of Midwestern grain becomes substantially more attractive to buyers in Europe and Asia. For a nation focused on narrowing its trade deficit, the exchange rate is probably the most efficient lever available. By making American exports price-competitive without sacrificing quality, the current administration is seeking to rebalance the trade ledger that has remained in deficit for decades.

Second, a "strong dollar" environment was a key catalyst for the offshoring of American industry over the last few decades. When the dollar's purchasing power is high, US firms find it cheap to build facilities and hire labour in emerging markets. The current policy seeks to invert this incentive structure, as a weaker dollar makes domestic labour and materials more cost-competitive on a global scale. A "Manufacturing Resurgence" is designed to shorten supply chains and insulate the US economy from the geopolitical fragilities exposed during the early 2020s and which look set to continue if not increase.

Third, for US-based multinational giants—the "Magnificent Seven" and their successors—a weaker dollar is an immediate tailwind for quarterly reporting. Since these entities generate a vast portion of their revenue in foreign currencies (Euros, Yen, and Yuan), those earnings "buy" more dollars when the greenback is weak. This dynamic provides a mechanical boost to the bottom line, effectively lowering the P/E ratios of major indices, making the US stock market appear more attractive to international capital and ensuring the US remains the world's deepest and most liquid financial market. Of course, President Trump will have one eye firmly on the level of the stock market in the run-up to November's mid-term elections.

Yet no monetary strategy exists in a vacuum, so what are the risks? The primary trade-off of a weaker dollar is the risk of imported inflation. As the US is a net importer, a drop in the dollar's value makes every imported product more expensive for the American consumer. The bigger risk, however, is one of velocity. Should the dollar's descent become a "disorderly sell-off," sovereign holders such as China or Japan may perceive the dollar's weakness as a signal of long-term instability. That may cause them to reduce or even dump their US Treasuries as part of a broader de-risking strategy. This capital flight could result in a "bond market rout", which would be very negative for markets and cause the Federal Reserve to intervene by raising rates, perhaps substantially, to protect the country's purchasing power. Raising the cost of debt for both the government and private corporations is the opposite of the administration's goals. Thus, any deliberate weakening of the dollar is a difficult yet vital thing to get right.

What does a structurally weaker dollar mean for portfolios? Historically, it has been the "starting gun" for Emerging Market rallies. In recent years, many EM central banks have maintained high interest rates to protect their currencies; as the dollar softens, these markets become magnets for "yield-hungry" capital, partly explaining their strong start to the current year. Multinational Quality Growth should also do well, as US firms with high foreign-revenue exposure will benefit most from a "repatriation tailwind." And of course, commodities are priced in dollars and so a weaker greenback typically leads to a rise in...you guessed it, gold. All of these potential impacts are adequately reflected, one way or another, in our thematic equity and alternatives allocations. How do you know if the dollar has fallen too far, or if it remains overvalued versus, say, the British pound? The traditional approach is to consider Purchasing Power Parity (PPP) theory. Also known as the Law of One Price, PPP suggests that in an efficient global market, a standardized basket of goods should cost the same regardless of the currency used.

The representative basket of goods and services it uses includes thousands of specific items (2,000-3,000) and is only updated annually. So whilst it might be comprehensive, it is static and painfully dull. Instead, let's look at some of the other proxies that have emerged to give a livelier but potentially just as accurate quick rule-of-thumb range.

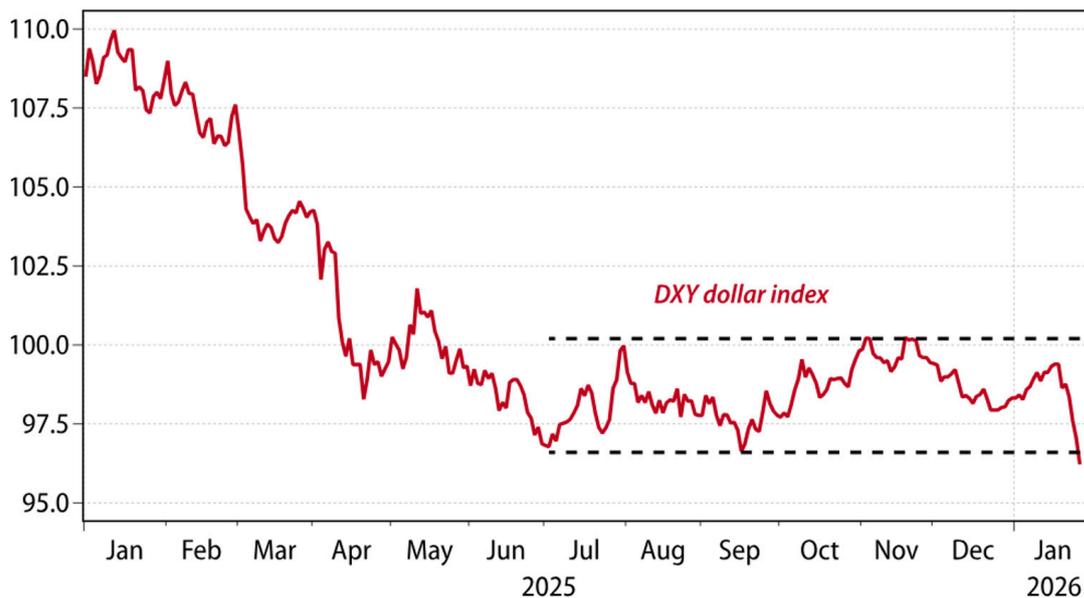
First, the "Mac Daddy": introduced by The Economist in 1986, the Big Mac Index (BMI) remains the "gold standard" of informal PPP. Since a Big Mac is identical in over 100 countries, its price reflects local inputs such as labour, rent, and agricultural commodities. With 40 years of data available, the BMI is also a great tool for identifying long term trends. When the BMI and the market rate diverge by more than 15%, history suggests a significant currency correction is usually on the horizon. It currently implies an exchange rate of \$1.30 per £1, and with the actual market rate at \$1.37, the index tells us the pound is overvalued relative to the dollar by roughly 5%, certainly within the acceptable range of uncertainty.

More adventurous Millennials, however, might be inclined to use the "Prestige" or iPhone index: if the Big Mac measures "local burger" costs, the iPhone Index measures "global trade" costs. Since an iPhone is a high-value item manufactured in a central location and shipped globally, its price should - in theory - be identical everywhere. At present, the rate implied by the iPhone index is a stark \$1.14 per £1. Fortunately for us, this is not a sign of a weak pound and an inevitable correction as much as it is a reflection of the "VAT Gap" - the UK's 20% Value Added Tax and higher logistics costs which create a "protectionist" pricing floor. Adding back the 20% VAT charge gets us surprisingly close to the current market level of \$1.37. In other words, the iPhone Index is a good barometer for regional tax burdens and trade barriers.

As for Gen Z, they might do away with anything physical at all and simply consult the "Digital" index: after all, in the modern economy, services are the new commodities. The Netflix Index removes physical frictions like beef and shipping and focuses purely on intellectual property. At \$1.38 per £1, the implied rate is almost perfectly aligned with the current market rate. This suggests that digital-first companies are more agile in their pricing than providers of physical goods, which is one of their major investment attractions. Netflix appears to be "absorbing" the cost of UK taxes to remain competitive, accepting lower profit margins in Britain to maintain subscriber growth. Which is exactly what the market wants to see.

Remarkably, whilst the Big Mac Index remains the most widely used and reliable alternative barometer, all of the above get us to within a surprisingly close range to the actual rate, suggesting the market is not too far out of sync with reality. Ultimately economics, unlike physics, is a social science of ranges and probabilities, not certainties. While we cannot pinpoint the exact "fair" exchange rate of the pound, these various indices—from burgers to bots—provide the boundaries of a sensible valuation and imply that the steady structural devaluation of the dollar is working. So far, so good. But easy does it.

The DXY has broken out to the downside



Gavekal Research/Macrobond

DISCLAIMER

Bentley Reid & Co (UK) Limited (FRN 572096) is authorised and regulated by the Financial Conduct Authority.

This communication is provided for information purposes only. Bentley Reid believes that, at the time of publication, the views expressed herein represent fair opinion; however, no assurance can be given that any illustrated or referenced performance will be achieved or repeated. All data and graphical information are believed to be accurate at the time of capture but may be subject to change and may not reflect current conditions. Fluctuations in exchange rates may cause the value of investments to rise or fall.

Recipients considering any action based on the content of this communication should seek independent advice from a professional adviser appropriate to their individual financial circumstances. Capital is at risk, and investors may receive back less than the amount originally invested. Neither the publisher nor any of its subsidiaries or connected parties accepts any liability for direct or indirect loss arising from reliance on, or use of, the information contained in this communication.