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15:50 EDT 05/06 Portfolios: CIBC Asset Mgment's Kalirai Eyes New Dlr Slippage

By Vicki Schmelzer

NEW YORK (MNI) - The currency market may have gotten a bit ahead of itself in attempting to price in future Federal Reserve tightening, which could mean renewed dollar weakness in the sessions ahead, said Harvinder Kalirai, vice president and currency manager at CIBC Asset Management.

The reality of the Fed remaining on hold for a lengthy period should mean a higher euro, although other currencies such as the Canadian and Australian dollars -- with commodity allure -- may see more demand, Kalirai said in an interview with Market News International.

"It's hard to see the Fed raising interest rates in the next six months," he said.

Even when the Fed does begin to tighten, typically it takes several months for the dollar to feel the positive effect. "It's too premature to start buying dollars at the moment," Kalirai said.

In the case of dollar-yen, trading at Y104.75 Tuesday, the U.S. interest rate advantage over Japan, currently at 150 basis points (fed funds versus overnight call rate) is likely to remain narrow for the next six to nine months.

"We view 400 basis points as critical," he said, "As long as we are under 400 basis points, it will keep the pressure on dollar-yen."

Kalirai did not rule out further euro slippage in coming months, but at the same time did not see a period of sustained euro weakness either. "I still would not be surprised to see the euro trade over $1.6000. It's more likely to move over $1.6000 than move below $1.5000," he said.

Nevertheless, CIBC Asset Management's purchasing power parity model puts fair value for the euro around $1.2500, which suggests the euro's topside should also be limited.

Back in November 2007, when the euro's fair value was about $1.2000, Kalirai spoke to Market News International about the euro's prospects at the time. Then, he reminded that after its inception in January 1999, the euro "undershot" by quite a bit, falling to $0.8225 in October 2000.

If the euro could fall nearly 40 "big figures" at a time when the dollar was rising, then it was logical to assume that the pair could climb 40 "big figures" during a period where the dollar was falling, he said. "Why can't we overshoot to the upside at $1.6000?" would be the thinking under this strategy, Kalirai said at the time.

Now, in 2008, while he remained more dollar bearish than bullish in the medium term, there should be a limit to euro strength. "I find it hard to see the euro over $1.6500 from a valuation perspective," Kalirai said. Euro-dollar was trading at $1.5530 Tuesday, down 3.1% from the record high of $1.6020 posted April 22.

Kalirai was especially upbeat about the Australian and Canadian dollar prospects, given the respective countries' solid fundamentals. "Commodities and commodity currencies are a win-win situation," he said.

If the U.S. economy recovers, it would likely prove positive for commodities and commodity country currencies. Conversely, if the U.S. economy declines and more Fed easing is seen, the dollar would likely decline and thus lift commodity prices, he said.

Kalirai was biased toward a dollar underweight against both the Aussie and Canadian dollars. "We like commodity currencies on valuation," he said. "We don't think these currencies are expensive, even relative to their current prices," he added.

When assessing a future currency trend, making simple historical comparisons is not always constructive, Kalirai said. As an example, the dollar-Canada, trading at C$1.0030 Tuesday, saw a low of C$1.1190 in 1991, he noted. Canadian inflation has been about 15% below U.S. inflation on a cumulative basis since 1991, Kalirai said.

Adjusting for inflation would make the C$1.1190 level about C$0.9512 -- not all that far from the 130-year dollar-Canada lows around C$0.9060 seen last November.

Canada has strong fundamentals, with abundant "food, energy and water" -- just what the global economy needs, Kalirai said. "I just don't see the Canadian dollar as overvalued," he said.

If commodity prices continue to firm, the loonie is likely to edge higher again. "That's our view - that over the medium term, say six to 12 months, dollar-Canada will be at the lows of last year, if not lower than before," Kalirai said.

At the same time, the Aussie dollar, hovering just under $0.9500 in afternoon action, should continue its march towards parity with the U.S. dollar, he said. "It all depends on what happens with commodity prices," Kalirai concluded.

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