The Impact of a Strong Dollar for Global Investors

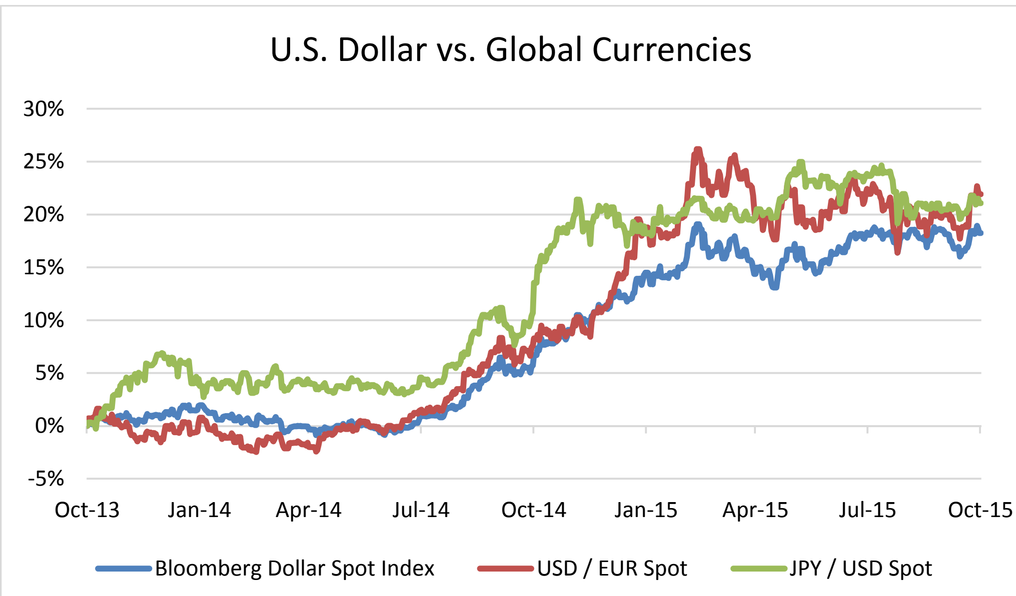
EDGE is an independent financial firm whose objective advice helps individuals and institutions realize their goals in the areas of investment management and corporate finance. The Edge Research Team's thoughtful and timely reports are based on extensive independent research and analysis of firms, financial developments, and macroeconomic trends.

EDGE Capital Partners
1380 W. Paces Ferry Road
Suite 1000
Atlanta, GA 30327
404.890.7707

AUTHOR
Howell Hollis

RESEARCH TEAM
Whit Davis
Stephen Halkos
Howell Hollis
Harry Jones
Brendan Keelan
Elizabeth Mackie, CPA
Jacobi Padgett
Dennis Sabo, CFA
Will Skeean, CFA

The U.S. dollar has strengthened against most developed and emerging market currencies over the last few years and appears poised to continue on this path. This can present consequences for both corporations and investors that deploy capital across the world.



Source: Bloomberg

The U.S. dollar has risen against a mixed basket of global currencies by approximately 12% over the last year and 20% over the last two years. This resulted from a number of factors, predominately a stronger economy relative to other developed regions coupled with expectations that the Federal Reserve will hike interest rates at the end of this year or beginning of next year. In contrast, other major central banks including the ECB remain focused on stimulating their economies by pursuing monetary easing policies.

The strength in the dollar can be a double-edged sword for domestic investors. For companies with material international revenue without offsetting costs the stronger dollar can be a headwind for profit translation. Companies with offshore manufacturing or production expenses are fortunate to have the ability to offset some of the revenue pressure, thereby preserving profits during a rising dollar period. For other U.S. companies that predominately generate revenue in the U.S. but manufacture overseas, the stronger dollar can be a blessing for corporate profits and stock prices. Many U.S. small and mid-capitalization companies fit this description. Adding to the complexity, many large multi-nationals hedge foreign exchange risk, a task that is made difficult by the velocity

The Impact of a Strong Dollar for Global Investors

and direction of exchange rate movements. During periods of FX volatility, investors have to do their homework to understand the repercussions to revenue and earnings growth.

In addition to the challenges presented above to individual companies, investors must also understand the implications of translating foreign investment gains back to their home currency, the U.S. Dollar. U.S. investors that omitted currency hedges have not fared as well in their European and Japanese investments due to the weakening Euro and Yen. For example, over the trailing one-year, a U.S. investor in the Nikkei Index without FX hedges returned 10% which compares to an 18% return in a hedged portfolio. Fortunate for U.S. investors, the innovation of Wall Street has resulted in a numerous investment vehicles that internally hedge foreign currency exposure, thereby preserving gains. It is important to note that hedges can work for and against investors in these vehicles so buyer beware.

Recent dollar strength is likely to continue should the U.S. Federal Reserve lift interest rates while foreign central banks continue to ease to support economic growth. This reversal has implications for both U.S. and global companies that have become accustomed to weakening dollar trends that have persisted until recently. Whether investors are analyzing individual companies or considering broader based international investments, it is important to consider currency exposure and hedging activity to preserve investment gains.