

EURO PARITY AND RISK MANAGEMENT

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For the first time since 2002, the euro has traded below [parity](#) with the U.S. dollar. While it has rebounded along with other risk assets back above a few times, concerns about the economic impact of the war in Ukraine pushed the euro down to its lowest levels in 20 years.

While euro/dollar parity may have important psychological implications, we know definitively that currency performance can have a significant impact on U.S. investor total returns in foreign markets.



Source: Bloomberg, as of 9/8/22.

Since the introduction of the euro on January 1, 1999, the currency provided positive returns in 10 out of 23 years (43.47%). Over the same time frame, equities in the region had positive performance in 14 out of 23 years (60.87%). On one hand, equities seem to trend higher over time. On the other, [developed market¹ currencies](#) can either appreciate or depreciate as they mean-revert toward fair value. Below, we examine four scenarios that try to separate [equity risk](#) from [currency risk](#) to try to understand which risks may be worth taking.

Scenario 1: Positive Calendar Year Returns for MSCI EMU Index and the Euro

Year	EUR/USD	MSCI EMU Index (Local)	MSCI EMU Index (USD)
2003	20.04%	19.10%	43.15%
2004	7.61%	12.67%	21.41%
2006	11.38%	21.92%	36.29%
2007	10.55%	7.82%	19.55%
2009	2.51%	27.32%	31.41%
2012	1.79%	19.31%	21.17%
2013	4.17%	23.36%	28.93%
2017	14.15%	12.63%	28.07%

Past performance does not guarantee future results. You cannot invest in an index. MSCI EMU Index: A free float-adjusted market capitalization-weighted index designed to measure the performance of the markets in the European Monetary Union.

When [risk has been “on,”](#) the euro and [stocks](#) have historically tended to appreciate together. This has had the added benefit of magnifying gains for U.S.-based investors. While the magnitude of gains has also been significantly higher for equities than EUR/USD, four out of eight years saw a double-digit appreciation for the euro. On its face, it seems that if an investor is [bullish](#) on European stocks, they should also be bullish on the currency.

Scenario 2: MSCI EMU Index and EUR down

Year	EUR/USD	MSCI EMU Index (Local)	MSCI EMU Index (USD)
2000	-6.31%	-2.54%	-8.72%
2001	-5.64%	-18.29%	-22.51%
2008	-4.24%	-44.85%	-47.57%
2011	-3.16%	-14.89%	-17.64%
2018	-4.48%	-12.75%	-16.90%
YTD	-12.08%	-17.13%	-27.41%

YTD: 12/31/21–9/8/22. Past performance does not guarantee future results. You cannot invest in an index.

However, it seems that positive [correlation](#) can cut both ways. In years where European equities were down, the euro also tended to be down, thus magnifying losses for U.S. investors. In years with double-digit [corrections](#) in equities, the euro depreciated on average by 5.1% per year. During more modest corrections, the euro depreciated by 6.3% per year. In terms of risk management, it seems [currency hedging](#) could be one way to potentially dampen [drawdowns](#) relative to an unhedged benchmark.

Scenario 3: MSCI EMU Index (Local) Up, EUR Down

Year	EUR/USD	MSCI EMU Index (Local)	MSCI EMU Index (USD)
1999	-14.26%	39.21%	18.77%
2005	-12.58%	25.38%	8.80%
2016	-3.18%	4.33%	1.34%
2019	-2.22%	25.45%	23.20%
2021	-6.93%	22.14%	13.54%
2010	-6.54%	2.40%	-4.25%
2014	-11.97%	4.32%	-8.39%
2015	-10.22%	9.82%	-1.42%

Past performance does not guarantee future results. You cannot invest in an index.

In the most classic case for currency hedging foreign equities (years when stocks are up, but currencies are down), we see that at least one-third of the time, currency losses completely outstrip the gains in equities. Put another way, an investor can get the call right on equities, but still end up losing money.

Scenario 4: MSCI EMU Index Down, EUR Up

Year	EUR/USD	MSCI EMU Index (Local)	MSCI EMU Index (USD)
2002	17.95%	-33.77%	-21.94%
2020	8.94%	-1.00%	7.89%

Past performance does not guarantee future results. You cannot invest in an index.

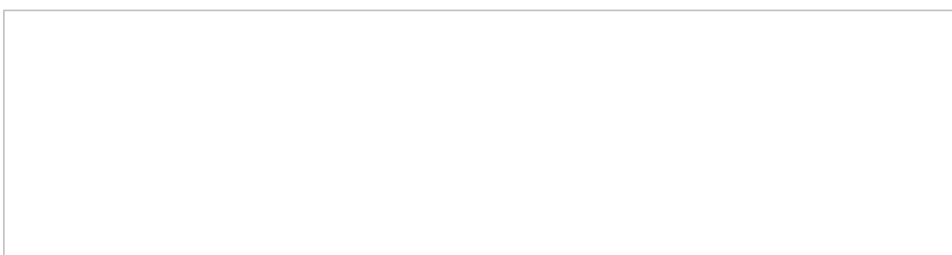
While anything is possible, when risk has been off, EUR has seldom been a safe haven, with the exception of 2002 and 2020. In these instances, a currency-hedged strategy underperformed in a down market.

FX-Hedged Exposure

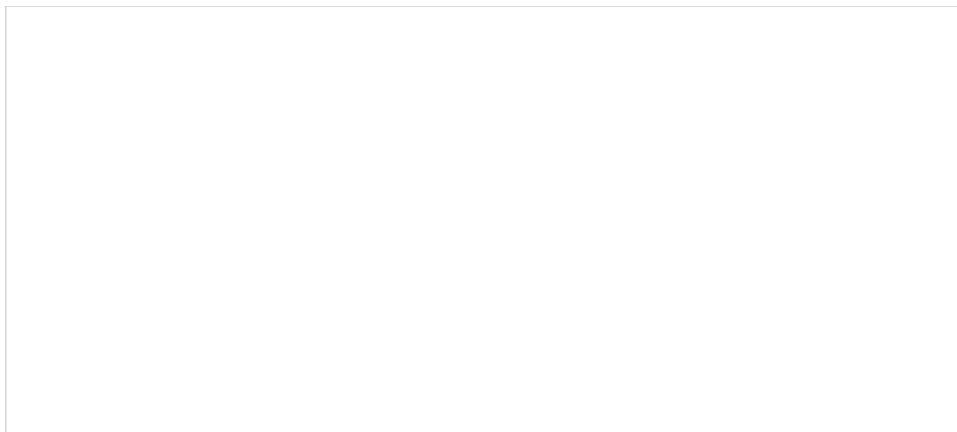
For investors who don't have a view on the direction of the euro or think the dollar will continue to strengthen, a hedged option may be more suitable.

The [WisdomTree Europe Hedged Equity Fund \(HEDJ\)](#), which seeks to track the price and yield performance, before fees and expenses, of the [WisdomTree Europe Hedged Equity Index](#), was launched in 2012 and provides exposure to dividend-paying companies with an exporter tilt in the [eurozone](#). The Fund hedges exposure to fluctuations in the euro by investing in one-month forward currency contracts.

Returns



Standard Deviation



Additional Index information is available [here](#).

See the [Fund's page](#) for full performance, risks and other important information.

Currency-hedged strategies aim to isolate returns to stock performance in the local markets, without changes in the local currency. Comparing returns of the [MSCI EMU Local index](#) versus the USD version, an outperformance ranging from 175 to 1,017 [basis points \(bps\)](#) can be seen with lower [volatility](#) for all standardized periods. An even greater outperformance was generated for the WisdomTree Europe Hedged Equity Index over the same time frame, ranging from 345 to 1305 bps.

¹ Past performance is not indicative of future results.

Important Risks Related to this Article

There are risks associated with investing, including the possible loss of principal. Foreign investing involves special risks, such as risk of loss from currency fluctuation or political or economic uncertainty. Investments in currency involve additional special risks, such as credit risk and interest rate fluctuations. Derivative investments can be volatile and these investments may be less liquid than other securities, and more sensitive to the effect of varied economic conditions. As this Fund can have a high concentration in some issuers, the Fund can be adversely impacted by changes affecting those issuers. Due to the investment strategy of this Fund it may make higher capital gain distributions than other ETFs. Dividends are not guaranteed, and a company currently paying dividends may cease paying dividends at any time. Please read the Fund's prospectus for specific details regarding the Fund's risk profile.

For the top 10 holdings of HEDJ please visit the Fund's fund detail page at <https://www.wisdomtree.com/investments/etfs/equity/hedj>

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Related Funds

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IMPORTANT INFORMATION

U.S. investors only: Click [here](#) to obtain a WisdomTree ETF prospectus which contains investment objectives, risks, charges, expenses, and other information; read and consider carefully before investing.

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You cannot invest directly in an index.

DEFINITIONS

Parity : Euro at parity means the euro would be trading at rate of \$1 equals €1.

Developed market : A country that is most developed in terms of its economy and capital markets.

Currency : Currency in which the underlying index returns are calculated. Euros: The returns are calculated, and there is no currency conversion; resulting statistics result purely from the returns of the equities. U.S. dollars: The returns are calculated and then converted into U.S. dollars; resulting statistics are the result of a combination of the euro's performance against the U.S. dollar and the returns of the underlying equities.

Equity risk : A type of market risk that applies to investing in shares.

Currency risk : the risk that an investment will decline in value due to a change in foreign exchange rates.

Risk-on/risk-off : refers to changes in investment activity in response to perceived risk. During periods when risk is perceived as low, investors tend to engage in higher-risk investments. When risk is perceived as high, investors tend to gravitate toward lower-risk investments.

Stock : A stock (also known as equity) is a security that represents the ownership of a fraction of a corporation. This entitles the owner of the stock to a proportion of the corporation's assets and profits equal to how much stock they own. Units of stock are called "shares."

Bullish : a position that benefits when asset prices rise.

Correlation : Statistical measure of how two sets of returns move in relation to each other. Correlation coefficients range from -1 to 1. A correlation of 1 means the two subjects of analysis move in lockstep with each other. A correlation of -1 means the two subjects of analysis have moved in exactly the opposite direction.

Correction : A drop of 10% or greater in an Index or stock from a recent high.

Currency hedging : Strategies designed to mitigate the impact of currency performance on investment returns.

Drawdowns : Periods of sustained negative trends of return.

Eurozone (EZ) : Consists of the following 18 countries that have adopted the euro as their currency: Austria, Belgium, Cyprus, Estonia, Finland, France, Germany, Greece, Ireland, Italy, Latvia, Luxembourg, Malta, the Netherlands, Portugal, Slovakia, Slovenia and Spain (source: European Central Bank, 2014).

MSCI EMU Local Currency Index : captures large- and mid-cap representation across the 11 developed market countries in the EMU and provides local currency returns, which are not translated back to U.S. dollars.

Basis point : 1/100th of 1 percent.

Volatility : A measure of the dispersion of actual returns around a particular average level. nbsp;nbsp;