

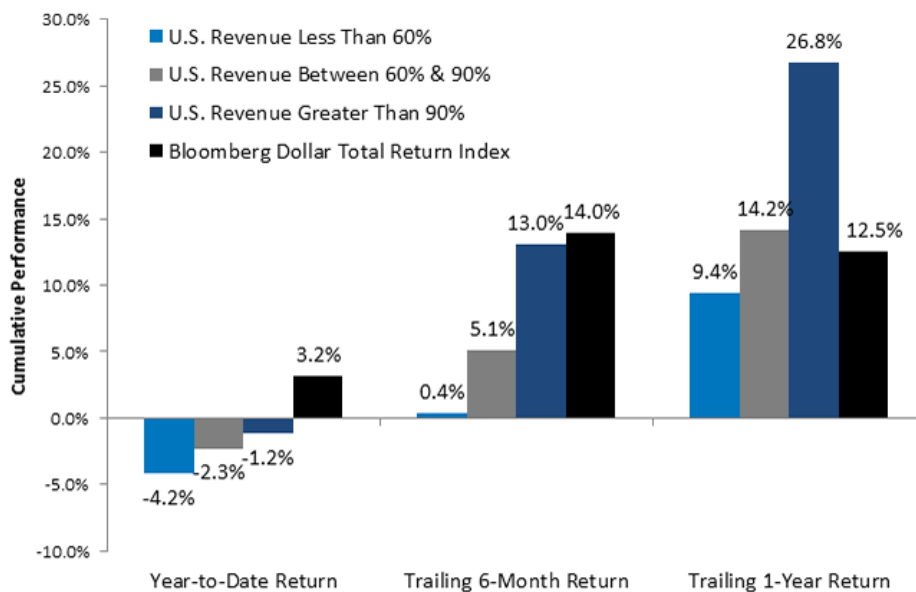
U.S. DOLLAR STRENGTH CONTINUES TO IMPACT U.S. MULTINATIONALS

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A few months ago, [we discussed](#) what a rising dollar means for investors' stock portfolios. In that piece, we pointed out that the [S&P 500 Index](#) has traded inversely to the currency moves over recent years, and it has become increasingly negatively [negatively correlated](#). One reason, we believe, is that a growing share of [revenue](#) and [profits](#) for U.S. corporations comes from overseas—and that share seems likely to increase with the globalization of the economy. Although currencies are not the sole driver of equity returns, we think that they are important to monitor, particularly now, given recent [central bank](#) actions. Some multinationals are still feeling the effects of the U.S. dollar strength, and the moves may persist. The most recent warnings are below: **The Procter & Gamble Company:**¹ "The October?December 2014 quarter was a challenging one with unprecedented currency devaluations," said A.G. Lafley, P&G's chairman, president and CEO. "Virtually every currency in the world devalued versus the U.S. dollar, with the Russian ruble leading the way." He also said, "The outlook for the year will remain challenging. [Foreign exchange \(FX\)](#) will reduce fiscal 2015 sales by 5% and [net earnings](#) by 12%, or at least \$1.4 billion after tax."² **Microsoft Corporation:**³ Amy Hood, Microsoft's CFO, estimated that, "In total, we expect that FX will negatively impact revenue growth by approximately 4 percentage points in Q3." She also said, "Our guidance is based on our current view of FX rates. Should the U.S. dollar strengthen beyond those assumptions, as it did this quarter, we would see additional negative impact to earnings, revenue, our balance sheet and our contracted-but-not-billed balance."⁴ **The Impact on Performance** While it can be difficult to quantify the exact revenue and profit impact across the globe from currency moves, we wanted to see if any performance trends might be visible over the past year. The [median](#) performance of domestic [large-cap dividend payers](#), grouped by U.S. revenue percentage, shows that the U.S. dollar hurt the performance of global multinational firms trading in the United States over the past year.

Median Performance by Revenue Ranges



Sources: WisdomTree, FactSet, 1/31/14–1/31/15

Universe of securities is the WisdomTree LargeCap Dividend Index. Past performance is not indicative of future results.

You cannot invest directly in an index.

• High U.S. Revenue

Performed Better: Companies with higher domestic revenues or lower international revenues do not see a revenue hit from a stronger U.S. dollar. If these companies import goods from abroad, their costs are actually reduced as the U.S. dollar gains strength. Financials, which includes real estate, and Utilities tend to have the highest percentages of domestic revenue; therefore they are not as negatively impacted by a strengthening dollar. These two sectors have also benefited from the decline in U.S. [interest rates](#) over the past year and saw very strong performance over the last year, significantly more than the global-export-oriented firms.

• Low U.S. Revenue Performed Worse: Companies with lower domestic revenues or higher international revenues are typically affected more by currency movements because they have to adjust their earnings based on these movements. This group is primarily made up of multinational companies in the Information Technology, Health Care and Consumer sectors. Firms in these sectors, like Microsoft and Procter & Gamble, highlighted above, have recently reported negative currency impacts and warned about future impacts if the dollar continues to strengthen.

Who Benefits from a Strengthening Dollar? • International Equities: Foreign multinational companies have the potential to benefit from a strengthening dollar because their products become less expensive to U.S. consumers, which could increase sales. These companies also benefit as their foreign sales are translated back to their home currency through a more favorable [exchange rate](#), resulting in higher earnings. We think that this is why developed international equities have historically performed better in periods when their currencies were weakening than in periods when they were strengthening.⁵ Even though a stronger U.S. dollar and weaker euro or yen might improve the profits of European or Japanese companies, the dollar strength can drag down the total returns of U.S. investors who do not [hedge](#) their international equity exposure. In a future blog post, we will examine the performance differential in exporters across different developed regions.

¹The Procter & Gamble Company was a 1.93% weight in the WisdomTree LargeCap Dividend Index as of 1/30/15. ²Source: The Procter & Gamble Company, Q2 2015 fiscal year earnings press release, 1/27/15. ³Microsoft Corporation was a 2.59% weight in the WisdomTree LargeCap Dividend Index as of 1/30/15. ⁴Source: Microsoft, Q2 2015 fiscal year earnings conference call, 1/26/15. ⁵Sources: WisdomTree, Bloomberg, 12/31/69?12/31/14.

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DEFINITIONS

S&P 500 Index : Market capitalization-weighted benchmark of 500 stocks selected by the Standard and Poor's Index Committee designed to represent the performance of the leading industries in the United States economy.

Negative correlation : Indicated by a tendency of two series of data to move in opposite directions. Shown in the chart (in the red box), the USD-to-GBP exchange rate is trending downward while the FTSE 100 Index is trending upward.

Revenue : Income that a company receives from its normal business activities, usually from the sale of goods and services to customers.

Net profit : A measure of profitability after accounting for all costs.

Central bank : Refers to the the monetary authority of any country.

Foreign Exchange (FOREX, FX) : The exchange of one currency for another, or the conversion of one currency into another currency.

Net income : A company's total earnings (or profit), which are calculated by taking revenues and adjusting for the cost of doing business, depreciation, interest, taxes and other expenses.

Large-cap dividend payers : The top 300 constituents in the WisdomTree Dividend Index ranked by market capitalization.

Interest rates : The rate at which interest is paid by a borrower for the use of money.

Exchange rate : The exchange of one currency for another, or the conversion of one currency into another currency.

Hedge : Making an investment to reduce the risk of adverse price movements in an asset. Normally, a hedge consists of taking an offsetting position in a related security, such as a futures contract.