THE Wealth REPORT

HOW THE STRENGTH OF THE DOLLAR IMPACTS THE MARKET

Overview

Up until 1973, the value of the U.S. dollar was determined by the Bretton Woods international monetary system. After 1973, the federal government decided to base the value of our currency on the economic principles of supply and demand. That also means that material commodities, such as oil and precious metals, are priced in dollars.

Economists use the terms "weak" and "strong" in the foreign exchange market as a means to compare relative value among different countries' currencies. When it comes to foreign investing, converting dollars to other currencies – such as euros and pesos – makes it easier to facilitate the buying and selling of dollar-denominated goods.

For investors throughout the world, the dollar is viewed as a reliable "safe haven" investment when other countries experience economic declines. By the same token, when the U.S. experiences a downturn, investors often sell U.S. dollars to recoup their losses.[2]

A strong dollar is frequently associated with a decline in stock prices, while weakness can lead to rising equities. However, currency valuation and its impact on the stock market generally is not quite that simple for investors.[1]

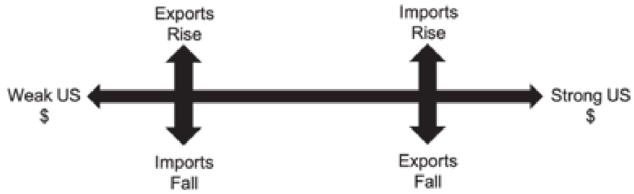
Relative Strength of the Dollar: Currency Exchange Rates[3]
As of March 4, 2019

US Dollar	**1.00**
Australian Dollar	1.41123
Brazilian Real	3.7717
British Pound	0.7567
Canadian Dollar	1.3291
Chinese Yuan	6.70448
Danish Krone	6.56105
Euro	0.87957
Hong Kong Dollar	7.84825
Hungarian Forint	277.68629
Indian Rupee	70.84
Indonesian Rupiah	14110.17387
Japanese Yen	111.89981
Mexican Peso	19.2464
New Zealand Dollar	1.46917
Norwegian Krone	8.57263
Polish Zloty	3.77907
Russian Ruble	65.88809
Saudi Riyal	3.74559
Singapore Dollar	1.35444
South African Rand	14.21421
Swedish Krona	9.25571
Swiss Franc	0.99843
Taiwan Dollar	30.84669
Thai Baht	31.68153
Turkish Lira	5.36759

Impact on Trade

As the U.S. works to negotiate new trade agreements with other countries, it's important to understand how currency valuation can influence the volume of imported and exported goods. For perspective, consider that a strong dollar means its exchange rate is higher than other currencies, and therefore can buy more of the foreign currency than before.[4] When the dollar is weak, imports become more expensive – especially when you tack on extra tariffs – which can reduce volume demand.

Trade Volume Based on U.S. Dollar Valuation



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Impact on Businesses

Because the value of the dollar rises and falls based on market demand and supply, it affects how businesses, manufacturers and farmers price their products. For example, if a domestically made product requires imported foreign raw materials, the price of those materials will likely change the price of the finished product. Sometimes companies absorb such extra costs to offer a fair and consistent price to consumers, but many times higher-priced raw materials will result in a higher price for the finished good.

On the other hand, when the cost of raw goods drop, companies have two choices. In some industries, companies are prone to keep prices the same and pocket the extra profit. Alternatively, a company can decide to reduce the price to increase volume sales.[5]

It's also worth noting that some businesses may change their marketing strategy based on the value of the dollar. When the dollar weakens, it may become more profitable to sell a higher volume of exports to foreign countries, so they refocus marketing dollars offshore.

Impact on Global Investors

A weaker dollar tends to generate higher profits for multinational companies because their products cost less in foreign markets. When U.S. companies export goods out of the country, they end up being cheaper for foreign consumers. Those lower prices tend to increase demand which leads to increased revenues, increased profits and an increased stock price for investors.

Furthermore, when those companies exchange foreign currency from international sales back into U.S. dollars, fewer dollars are exchanged for the stronger currency, which can result in higher domestic profits and, consequently, share value.

Conversely, a strong domestic currency hamstrings exports and makes imports more appealing, resulting in lower sales (profits and share value) for domestic companies.[6]

If the U.S. dollar continues to appreciate, fewer U.S. exports could lead foreign consumers to switch brands and rely less on American goods. Long term, that can have a negative impact on company profits and share prices.

Industry sectors that tend to be more detrimentally impacted by a strong dollar include basic materials, energy and technology.[7]

Impact for Domestic Investors

Shortly after Americans elected pro-business President Donald Trump, the U.S. dollar rose to its highest level in years. However, diverging sentiment regarding the Administration's tax and international trade policies has triggered substantial fluctuation during the past two years. Despite this reaction, it is important to reiterate that the value of the U.S. dollar is not tied to the U.S. economy or administrative policies – it is directly linked to the value of currencies in other nations.

The strength or weakness of the U.S. dollar is more likely to impact investors of foreign companies, particularly with regard to international currency trades. Domestic investors looking to reduce risk may want to stay away from multinationals and focus on companies with primarily domestic exposure. Bear in mind that while this may reduce currency risk, it could increase risk of loss due to the lack of diversification.[8]

"Every 7- to 8-percent move in the dollar results in a 1-percent move in the opposite direction for U.S. corporate profits."[9]

Final Thoughts

Moving forward, U.S.-foreign trade agreements and the uncertainty surrounding Brexit make it difficult to predict the future of the U.S. dollar relative to other currencies. Then again, investment decisions are usually driven more by financial goals, timelines and individual tolerance for risk, so the strength of today's dollar may not provide reason enough to change one's strategic asset allocation.

With that said, it's a good idea to discuss any concerns you may have with your financial advisor. He or she can weigh the potential effects of currency movements on your portfolio to determine if changes would be prudent relative to your circumstances.

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[1] Zack's. Jan. 28, 2019. "Do Stocks Rise When the Dollar Falls?" https://finance.zacks.com/stocks-rise-dollar-falls-9961.html. Accessed Mar. 4, 2019.
[2] Ibid.
[3] Oanda. March 4, 2019. "Currency Rates Comparison Table." https://www.oanda.com/currency/comparison. Accessed Mar. 4, 2019.
[4] Osikhotsali Momoh. Investopedia. Feb. 6, 2019. "What do the terms weak dollar and strong dollar mean?" https://www.investopedia.com/ask/answers/06/strongweakdollar.asp. Accessed Mar. 4, 2019.
[5] Fraser Sherman. Bizfluent.com. Nov. 21, 2018. "What Happens to Exports & Imports When the Dollar Appreciates & Depreciates?" https://bizfluent.com/info-8221802-happens-imports-dollar-appreciates-depreciates.html. Accessed Mar. 4, 2019.
[6] Misyrlena Egkolfopoulou, Liz Capo McCormick and Cécile Daurat. Bloomberg. Nov. 5, 2018. "Dollar Vortex Puts Chill on Earnings That May Worsen in Spring." https://www.bloomberg.com/news/articles/2019-02-03/dollar-vortex-puts-chill-on-earnings-that-may-worsen-in-spring. Accessed Mar. 4, 2019.
[7] Osikhotsali Momoh. Investopedia. Feb. 6, 2019. "What do the terms weak dollar and strong dollar mean?" https://www.investopedia.com/ask/answers/06/strongweakdollar.asp. Accessed Mar. 4, 2019.
[8] Ibid.
[9] Misyrlena Egkolfopoulou, Liz Capo McCormick and Cécile Daurat. Bloomberg. Nov. 5, 2018. "Dollar Vortex Puts Chill on Earnings That May Worsen in Spring." https://www.bloomberg.com/news/articles/2019-02-03/dollar-vortex-puts-chill-on-earnings-that-may-worsen-in-spring. Accessed Mar. 4, 2019.