Quarterly Newsletter

Roth FINANCIAL PARTNERS

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The Dollar

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When we think of “dollars,” we usually think of the physical green bills that we keep in our wallets or purses (or are crumpled up in the back of our jean pockets.) Physical dollars have become less and less integral in our day-to-day lives with the advent of technologies that allow digital transactions like Venmo or Zelle and the increased use of debit & credit cards. However, we also hear about “the dollar” in terms of its strength or weakness, especially in connection with other currencies, like the Euro and the Japanese yen. Do we want the dollar to strengthen or weaken? Well, it depends a lot on the situation. When we think about the impact of changes in the strength of the dollar, we need to consider potential ramifications between economic and portfolio impacts. (As a quick aside, the term “dollar” is used in several different currencies, including those in Australia, Canada, and New Zealand – going forward, we’re particularly discussing the US dollar.)

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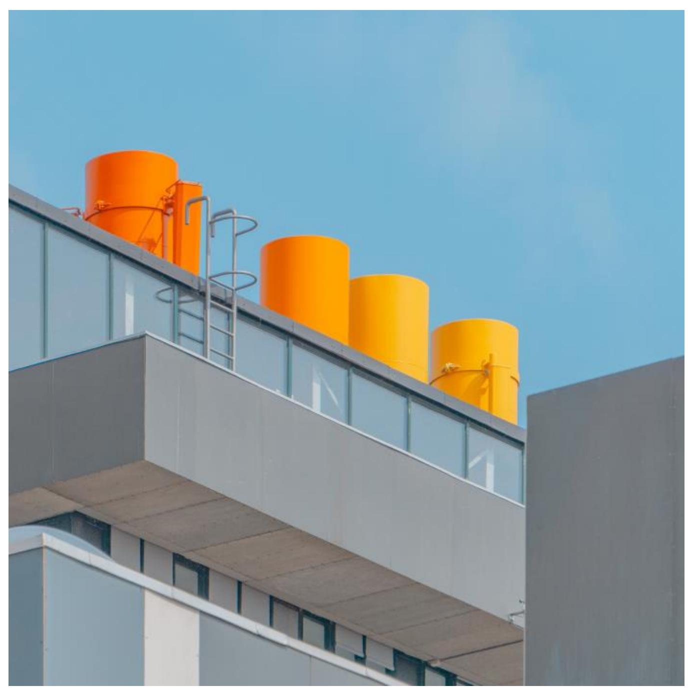
It is common for the strength of the dollar to be used for political means as well, standing in for the strength of the US as a whole. Recent events, such as the sanctions placed on Russia following its invasion of Ukraine as well as talk of using Chinese currency to price some oil transactions with Saudi Arabia, are enflaming rhetoric about whether the reign of the dollar as the world's "reserve currency" is soon to pass. Below, I'm hoping to avoid political ramifications because the extreme hypotheticals are used by political actors to rile up constituents on both sides for political purposes (and as we say consistently, separating politics and portfolios due to the emotions brought up by the former is very important.)

In the 20th century, the dollar took over as the global reserve currency from the United Kingdom's pound sterling due both to the US' ability to "weather the storm" of both World Wars better than almost any other major economy as well as some cunning behind-the-scenes politicking during the establishment of the 1944 Bretton Woods agreement towards the end of World War II (allowing for the convertibility of foreign currencies into dollars at a pegged value).

Since the US produces roughly a quarter of all world output, it plays a large role in the global economy. Because of that role, countries around the world have accumulated dollar-denominated financial assets. As of the end of 2022, the dollar made up almost 60% of world reserves, a percentage that has held fairly steady for the past twenty years. Foreign countries have accumulated such assets due to a belief in the stability of the dollar and its use as a "safe haven" asset during times of crisis (such as March 2020). Even if countries diversify their reserves into other currencies (especially those countries with which the US is not ultra-chummy), the fact that the dollar is freely convertible (unlike the Chinese renminbi, which has strong capital controls by the Chinese government) and has deep and liquid bond markets gives it a leg up as the premier global reserve currency.

At a very general level, it is easy to make the assumption that a strong dollar = being better for Americans. In certain cases, that is true. The strength of the dollar has allowed for both the US government and US-domiciled companies to issue debt cheaply. With a stable currency and a decreased level of uncertainty, there is less need for additional risk premiums related to currency risk to be embedded in the interest rate of such securities. For you world travelers, if you're a US tourist visiting Europe, you would love a stronger dollar, as it means that when you convert your dollars to euros to buy a couple of lattes, your stronger currency is able to buy a little more coffee (so go ahead and get that extra shot of expresso!)

On the flip side, if a stronger dollar is better for Americans to go abroad, doesn't that also mean that it is more expensive for foreign visitors to visit the United States, thereby hindering the domestic travel industry? Similarly, what if you ran a US company that was hoping to "go global" and start making in-roads in the European or Asian markets? A strengthening dollar would be a hindrance to your bottom line, as when you earn foreign currencies through foreign sales and then try to convert them back to dollars to pay your domestic bills (salaries, rents, etc.), your foreign currency is worth less and your profits (in dollars) are negatively impacted. Domestic manufacturing has dealt with plenty of headwinds over the past decades due to a strong dollar. Goods made outside of the US are much more attractive (cheaper) due to such dollar strength, causing our trade deficit (the difference between what Americans buy from abroad and what Americans sell abroad) to increase 82% over the past ten years. In fact, the US has now run a current account trade deficit for 31 straight years! With the US being such a consumer-centric economy, we as consumers have benefitted greatly from the strong dollar. But if domestic manufacturing gets a little lift from a somewhat weaker dollar, is that such a bad thing?



Like most things in life, trade-offs in the currencies are apparent and must be considered. Keep that in mind whenever the strength or weakness of the dollar is being discussed in passionate terms.

How This Translates to Portfolios

From a portfolio perspective, one of the reasons we feel strongly about investing in a globally diversified basket of stocks relates to the currency diversification benefits of holding non-US equities. A weaker dollar tends to act as a tailwind for the returns of non-US stocks, as their values are worth more upon being converted to the dollar. On the flipside, a stronger dollar can play a role in holding back international stock returns in relation to their US counterparts (as has been the case in the past decade.)

Let's look at a couple of examples, but first let's introduce our "cast of characters" in describing how the strength of the dollar impacts global returns:

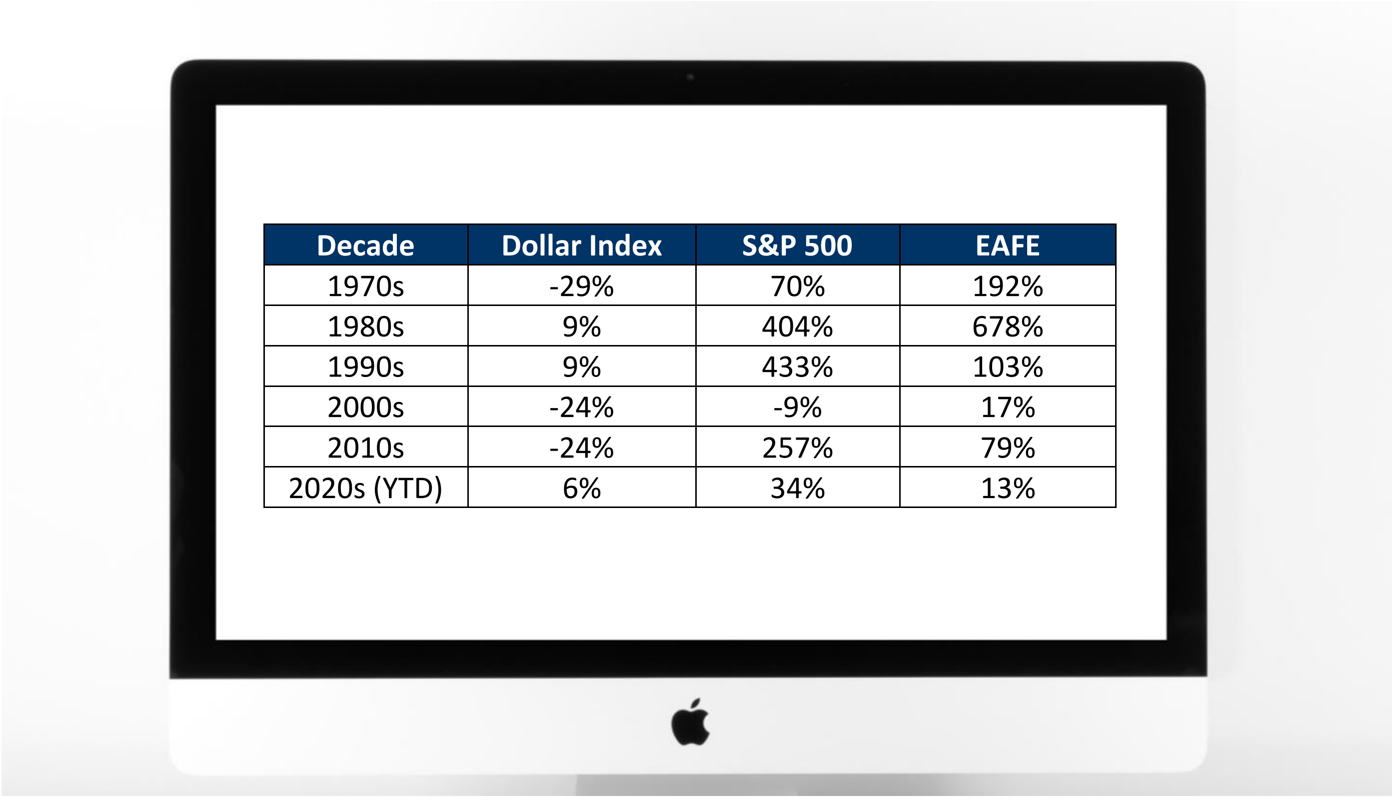
1. The Intercontinental Exchange US Dollar Index ("Dollar Index") is an index calculated from the weightings of the following six currencies against the dollar. If this value goes higher, then we would say the dollar is strengthening against these currencies.
    a. Euro (57.5%)
    b. Japanese Yen (13.5%)
    c. British Pound (12%)
    d. Canadian Dollar (9%)
    e. Swedish Krona (4%)
    f. Swiss Franc (4%)

2. MSCI EAFE Index ("EAFE") is an index that tracks larger companies in developed countries around the world, but outside of the United States (EAFE stands for Europe, Australia/Asia, and the Far East.) These countries include Japan, the UK, France, Switzerland, and Germany.

3. MSCI EAFE Local Currency Index ("EAFE Local") is the same index as the above but noted in terms of the countries' local currencies. This takes the impact of currency changes out of the return equation.

4. S&P 500 Index ("S&P 500") is an index that tracks the 500 largest publicly traded companies in the United States.

Below is a table of decades since the early 1970s, listing total returns for each of indices (the 1970s begin in 1971, due to data constraints):



Decade	Dollar Index	S&P 500	EAFE
1970s	-29%	70%	192%
1980s	9%	404%	678%
1990s	9%	433%	103%
2000s	-24%	-9%	17%
2010s	-24%	257%	79%
2020s (YTD)	6%	34%	13%

On a high level, there appears to be a clear pattern in decades when the dollar rises, the S&P 500 (standing in for US stocks) has a leg up, while the opposite occurs in decades with a falling dollar. The 1980s stand in contrast with this "rule of thumb," as the dollar appreciated for the decade, but international stocks outperformed US stocks by almost 300%. However, this was mostly due to two reasons:

1) the dollar split the decade with a meteoric rise from 1980-February 1984 of over 90% appreciation in the period and then a rapid fall through the rest of the decade, ending the 1980s down 43% off its high and only up 9% for the decade and

2) Japanese stocks went haywire, increasing 1,114% over the decade which heavily skewed the EAFE index (the EAFE without Japan "only" went up 359% for the decade.) On a side note, Japanese stocks are only up 23% in total (less than 1% annually) in the over thirty years since that crazy decade - a common example used for why investing in the equities of a single country (even one that has performed so well as of late) can be dangerous.

In a more recent example, let's look at last year. In 2022, international stocks as measured by the EAFE index decreased 14% (including dividends), outperforming the S&P 500 index, which decreased 18%. But let's breakdown the year into two parts:

Part 1) The first three quarters (1/1/22 – 9/30/22) and

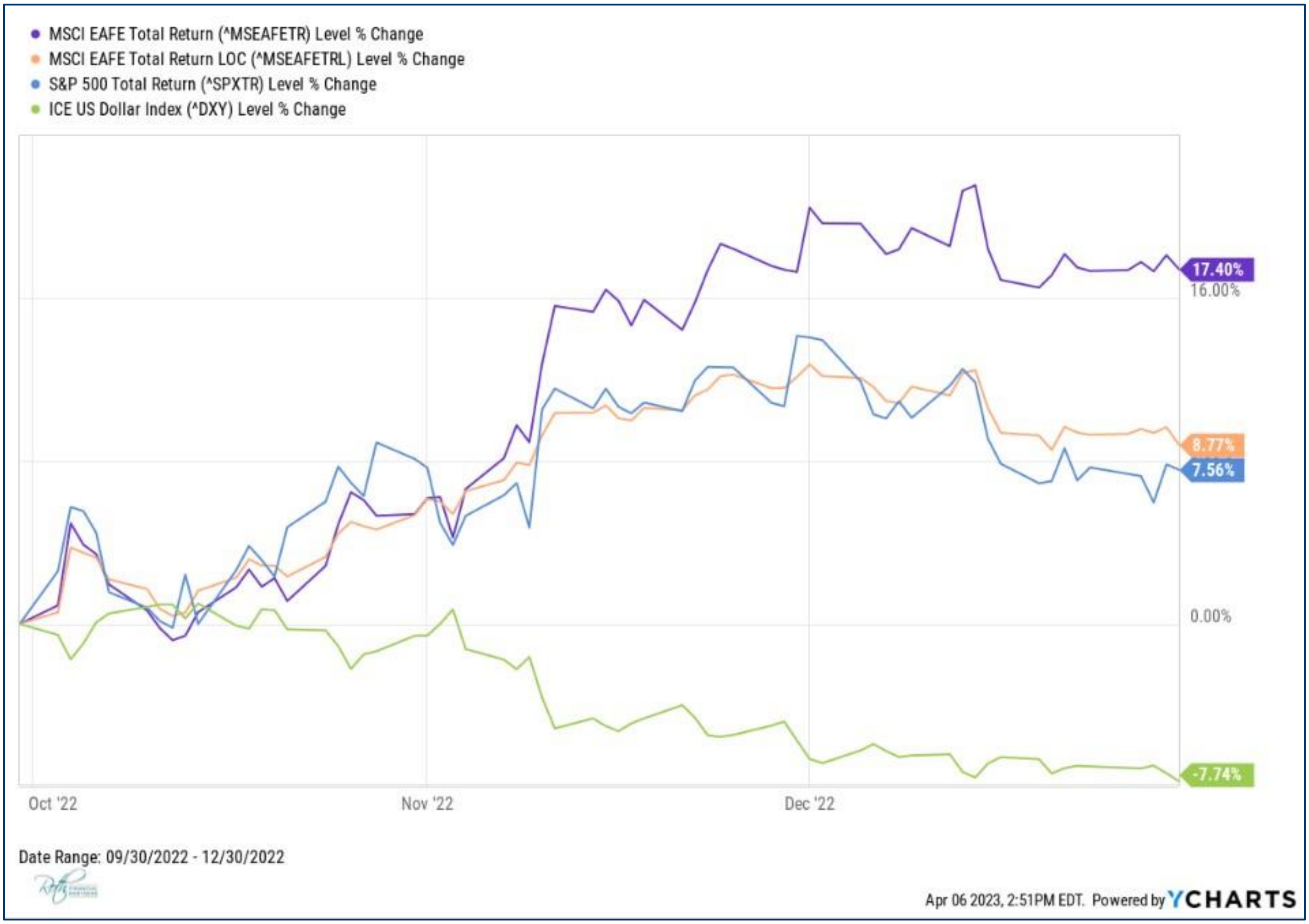
Part 2) The fourth quarter (10/1/22 – 12/31/22).

Part 1) The First 3 Quarters (1/1/22 – 9/30/22)

Through the first three quarters, returns for these major indices looked even uglier than where things ended up. Through Q3, the S&P 500 was down 24% while the EAFE index was down almost 27%. At the same time, the Dollar Index had strengthened 17% due to the Fed leading the pack in interest rate increases and global economic concerns leading to a flight to the safety of the dollar. Due to the strengthening of the dollar, we can expect that the EAFE Local index would outperform the EAFE index, since the former does not take into consideration the currency impact – and we would be correct, as the EAFE Local decreased 14% through three quarters, outperforming both the S&P 500 and the currency-impacted EAFE.

Part 2) The 4th Quarter (10/1/22 – 12/31/22)

In the fourth quarter of 2022, however, the tide shifted decidedly, with the dollar weakening almost 8% and the EAFE index (up 17%) outperforming the EAFE Local index (up 9%), as well as the S&P 500 (up 8%), handedly.



Similar to how we do not think we can predict short-term stock market movements or where interest rates will be in the next couple of months, we think it's near impossible to consistently forecast exchange rates in the currency market, which are open 24 hours a day and are the largest market via trading volume in the world. We believe it is especially important to diversify equities globally, with one particular reason being that if there is any drawn-out weakness in the dollar, a portfolio can potentially benefit from the tailwind for international stocks.

A Few Reminders

Client Access

For accounts that are custodied at Raymond James (our main custodian for accounts that we discretionarily manage), you can log into Raymond James Client Access at clientaccess.rjf.com (or download an app in your preferred App Store) to view your account balances, retrieve account statements and tax documents, and upload items to send to us securely via the Vault. If you (or your spouse that also has an account custodied at Raymond James) currently do not have a Client Access account, we highly recommend you do so, both to keep track of your account and stay abreast of how your portfolio is allocated, but also for the ability to toggle document delivery settings.

There are multiple types of documents that are required to be sent to you by Raymond James and you can decide whether you prefer to receive them either (i) in the mail or (ii) "e-delivery" via email notification for you to log in and view. Document types include:

1. Account Statements.
2. Trade Confirmations.
3. Tax Reporting (everyone's favorite!).
4. Reports & Proxies/ Prospectuses – examples: these could be official reports from fund companies, which are required to be sent to any investors, or any voting items for individual company securities.
5. All Other Correspondence.

From a cost and "earth-friendly" perspective, Raymond James would love for all documents to be e-delivery, but we understand that sometimes you prefer to read items on paper (and so do we!) One item that we recommend is for trade confirmations to be set to e-delivery, as with the increased usage of money-market funds due to current interest rates, we are more often purchasing money-market shares with excess cash (even in smaller quantities) and thereby entering in more trades than has historically been the case. Whatever you decide from a delivery perspective, we also highly recommend you sign into Client Access at least every six months, or all of your delivery settings may be reset to paper (from Raymond James' perspective, it is for your benefit, as from a compliance perspective they want to make sure you know what and how you're invested.)

Cash Distribution Needs

A final reminder relates to cash needs. For your protection, we are required to vocally verify any cash distribution requests you may have from your portfolios. If you send us an email requesting a distribution, we are going to need to "hear your voice" to move forward with the request – therefore, please consider giving us a call in lieu of (or in addition to) an email for such requests – plus we would love to say hello anyway!

Around The Office Updates

Looking Into Q2

Copies of Tax Returns

If we have not already received a copy of your 2022 tax return, we would like to get a copy from you at your convenience. This allows us to maintain updated information as it relates to your financial plan.

New Office Space!

As you may have heard, we have built our own new office building across the street from our current location, and we are getting very excited to move in. Our target move date is Friday, May 19th! We will send out a formal email to everyone with details (including the new address) a few weeks prior to the move. Our contact information (Phone number/ email addresses/ etc.) will remain the same. We cannot wait to show you the new space!

They are a Handful!

As you can tell, Jimmy and Sandi have their hands full! Kaylee (5), Maggie (3), and Casey (2 months) are *non-stop.* The good news is that the kids surprisingly sleep well at night. The bad news is that the kids sleep well at night and are locked and loaded with energy during the day! Lots to be thankful for!

It's The Most Wonderful Time of the Year!

To celebrate Opening Day, and our 2022 World Series Champions: The Astros, Eric and boys took their annual opening day photo. As you can see, Abe (3) and Jonah (1) were absolutely thrilled. We know that this is a sign of good things to come. Go Astros!!