



Plenty of upside in downward dollar

Australians planning an overseas holiday may be lamenting the fall in the dollar, but for investors and much of the country there are plenty of positives. As a nation heavily reliant on exports the weaker dollar makes us more competitive and helps to underpin much needed economic growth.

Investors with exposure to international equities and domestic companies with offshore earnings are likely to be major beneficiaries of the more favourable exchange rate.

The decline against the US dollar to its lowest level in four years will be particularly welcomed by the Reserve Bank which has talked about the currency being uncomfortably high for some time.

The Aussie dollar was trading at about US87c in early November, down from US94c in early September and well off its all-time high of US\$1.10 in May 2011.

To put the recent currency moves in perspective, the Australian dollar against the US dollar has averaged about US76c since the dollar was left to market forces, or floated, in 1983.

Some analysts predict that the currency is on its way back to that long term trend, with the current strength in the US dollar a significant driving factor.

Currency winners

While accommodation and shopping in the US or Europe may not be as cheap as it was for Australian travellers, investors in companies with US or Euro dominated earnings should stand to benefit.

That's because any earnings generated in US dollars will be worth more to Australian investors.

Australian Dollar to US Dollar Chart - US Dollar per 1 Australian Dollar



Snapshot



Companies that manufacture or provide a service in Australia and compete with the now more expensive imports such as steel, fertiliser or tourism should also do well. Just some of the well-known companies in these sectors include BlueScope, Incitec Pivot and Crown.

The danger of expensive imports is rising inflation but there are also companies that stand to benefit from rising prices. For example, retailers such as Wesfarmers and Woolworths and toll-road operator Transurban Group could see expanding profit margins if inflation increases.

Product prices from biscuits to road tolls would increase with inflation. So provided a portion of these companies' costs remain fixed, profits should increase.

Companies that have production costs in Australian dollars but export products like natural gas and iron ore which are priced in US dollars also stand to benefit. These include Woodside, BHP Billiton and Rio Tinto.

A falling Australian dollar translates into higher Australian dollar revenue from the same US dollar level of goods sold. For example, every 1c fall in the Australian Dollar increases BHP's profit by US\$100 million.

Currency losers

Some of the sectors that may not be celebrating the falling Australia dollar include those that buy goods offshore, either for use in manufacturing or resale to Australian consumers.

Retailers including JB Hi-Fi will pay more for many of the electronics

such as flat screen TVs that households have been enjoying at record low prices.

The lower dollar could also hurt companies that have significant US dollar denominated costs, such as aviation gas in the case of Qantas.

Hedging your bets

Currency movements can translate into losses or gains on an international share portfolio depending which way the currency moves.

Just as companies will protect themselves against foreign currency movements by locking in or hedging costs like US dollar borrowings, investors can take the same precautions with their overseas investments.

If you invest in managed global share funds there is often a choice of hedged and unhedged versions. This allows you to take a view on where the currency is headed based on your investment time frame.

For example, if you think the Australian dollar will continue to rise you might choose a fund which has hedging in place. But if you think the dollar will fall you might choose an unhedged version and hopefully benefit when you convert your offshore earnings into Aussie dollars.

Just as there are challenges from a fluctuating currency there are also opportunities.

Call us if you wish to discuss how to position your portfolio for the falling dollar.



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