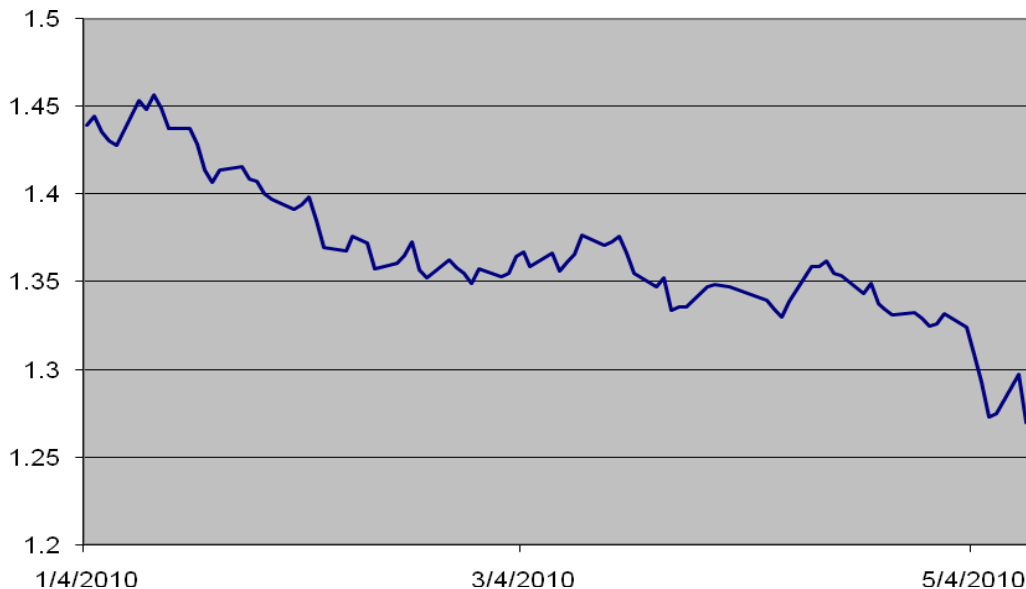


Why U.S. Investors Should Care About the Euro

By: *SEI Investment Management Unit*

Sovereign debt troubles continue to persist in Greece and other parts of peripheral Europe, resulting in volatile global markets and heightened anxiety. Despite the unveiling of a Greek bailout package by the European Union and the International Monetary Fund, investors are still signaling a lack of confidence by sending European markets lower. As uncertainty about the situation grows, it has begun to affect the European banking system as well. In response, the euro has fallen against the U.S. dollar from \$1.33 on April 30 to \$1.22 on May 26. Exhibit 1 highlights the euro's decline against the dollar since the beginning of the year. As of May 27, the euro has fallen below levels reached during the worst parts of the global recession.

Exhibit 1: The Euro's Descent, January 2010 to Present



Background

For many U.S. investors, this may seem like a small matter. After all, if one is invested primarily in domestic stocks and bonds, what difference does it make? The answer is that it can have a significant impact.

The past few decades have brought about massive global integration. Companies based in one country began to look at other parts of the globe for access to new employees as well as new customers. This trend resulted in increased exposure to foreign currency; for example, large U.S. companies are heavily exposed to international markets, deriving an average of 60% of their revenues

from sources outside the U.S. Of this 60%, 40% of revenues are tied to Europe, which translates into a 25% average exposure to Europe for large U.S.-based firms. For companies in the S&P 500 Index, about 10% of revenues come from Europe as a whole. For some companies such as IBM, Apple and Caterpillar, exposure to the euro is even greater—approximately 30%. Because the destinies of U.S. companies are increasingly tied to markets outside the U.S., the result is even greater volatility for U.S. securities during times of global economic crisis.

Our View

SEI believes that the euro will be vulnerable to further declines until more clarity is reached regarding bailout plans for Greece and peripheral Europe. While a declining euro would result in the U.S. being less competitive with regard to its exports, investors in dollar-denominated assets would benefit from currency appreciation.

Risks at this time include additional sovereign debt downgrades for nations such as Portugal and Spain, as well as increased political unrest and a flight to safety by investors. Anger is brewing in France and Germany as citizens take umbrage at funding their neighbors' bailout packages; at the same time, protests in peripheral Europe continue in response to dramatic budget-cutting efforts. At this time, the euro's role as a reserve currency is in serious jeopardy, and if it continues in this fashion, it may cease to be a barometer for the state of the global economy. We do not believe that the euro will reach parity with the U.S. dollar, but we continue to monitor possible outcomes resulting from this scenario. At this juncture, dollar-denominated investments have helped portfolio performance, and we believe positive economic news out of the U.S. will result in it continuing as the safe haven of choice for global investors.

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