Global Returns Under The Dollar's Rise And Fall

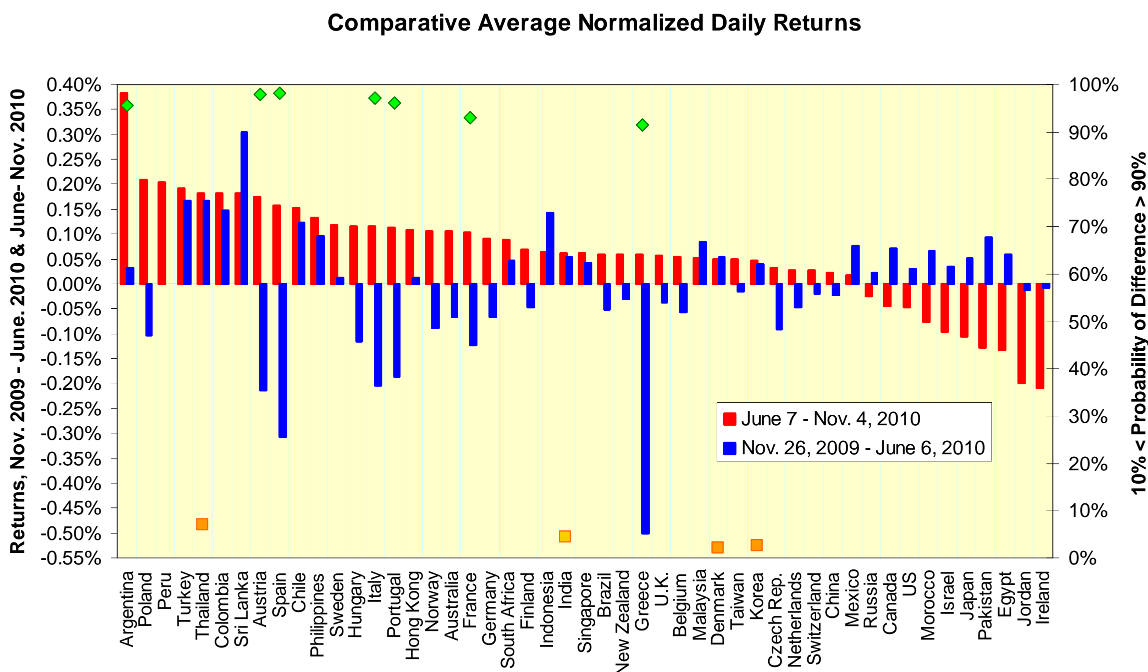
If you do not remember Thanksgiving 2009, please let me refresh your memory: Dubai managed to scare the markets by threatening default on their desert Disneyland and its various tributes to Ozymandias. That default scare reminded many things were not quite on the up-and-up in the Eurozone's periphery. Indeed, two of the five PIIGS have been placed on life support here in 2010, one 'G' and one 'I,' leaving just SIP.

The dollar, which had been taking it on the chin for much of 2009 to the delight of those entrusted with preserving its purchasing power, proceeded to rally by default, no pun intended. The dollar index (DXY), 57.6% of which is the euro, rose from 74.17 on November 26, 2009 to 88.708 on June 7, 2010. The market then decided the Eurozone was not going for a refreshing dip in the cesspool but the dollar just might given the money-printing proclivities of its managers. The DXY then sank back to 75.631 on November 4, 2010, at which point everyone was reminded of just how awful the euro was.

The dollar and the euro: They both could do better.

Comparing Equity Returns

This round-trip action gives us a simple and clean laboratory for comparing the performance of various national equity indices between the two periods. The chart below depicts the total returns in dollar terms for the first period (red columns) and second period (blue columns), sorted in descending order by the second period's returns.



Two sets of markets are added. Those in green denote the markets whose average returns between the two periods are different at a 90% confidence level; those in orange denote the markets whose average returns between the two periods are the same at a 90% confidence level.

The four markets whose average returns were near-identical are Thailand, India, Denmark and Korea. The seven markets whose returns were significantly different are Argentina, Austria, Spain, Italy, Portugal, France and Greece. This second list has six members of the European Monetary Union and one permanent basket case whose average daily returns really took off when its Peronist former president and husband of the current president dropped dead from a heart attack. This is quite the septet, no?

In all of the cases for the not-so-magnificent seven USD-denominated performance increased during the second period. The decline of the dollar had many effects, but one of the most direct and incontrovertible was a huge increase in the relative performance of selected EMU members. Ireland, a small market, was an exception here.

If you do not want to be bothered with the dollar's short-term gyrations, focus on those countries such as Thailand, India and Korea whose performance was indifferent to the greenback. If and when you think the dollar is going to take another downturn – and one is inevitable under the present combination at the Federal Reserve and the Treasury – go back to Europe.