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Independent Research Providers to the Professional Investment Community

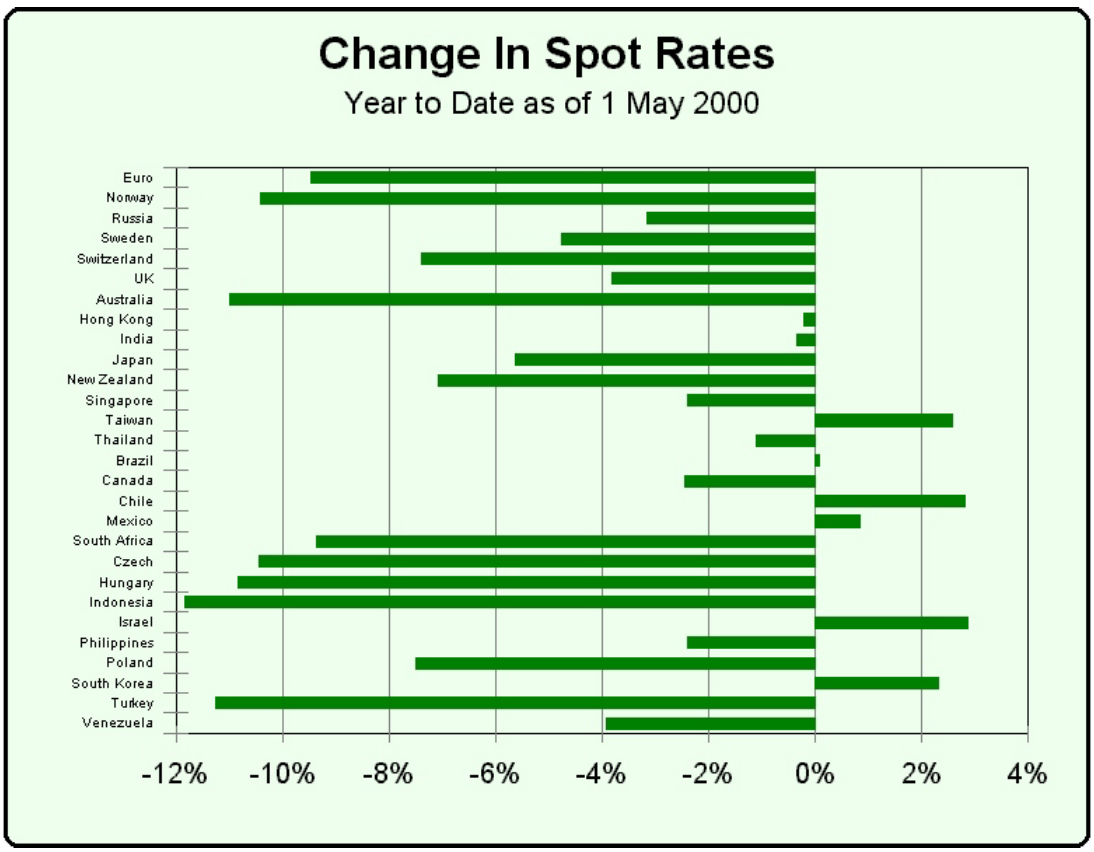
2 May 2000

Special Report

Spotlight on Spot Rates

Greenback Dominates

Only a Few Small Markets Outperform the Buck



Misery Loves Company

If you've been focusing on only a small number of currencies, you may not be aware that the decline you have likely been witnessing is quite typical. We have arrayed 28 different currencies on this bar chart so that you compare the performance so far in 2000 of a wide variety of markets.

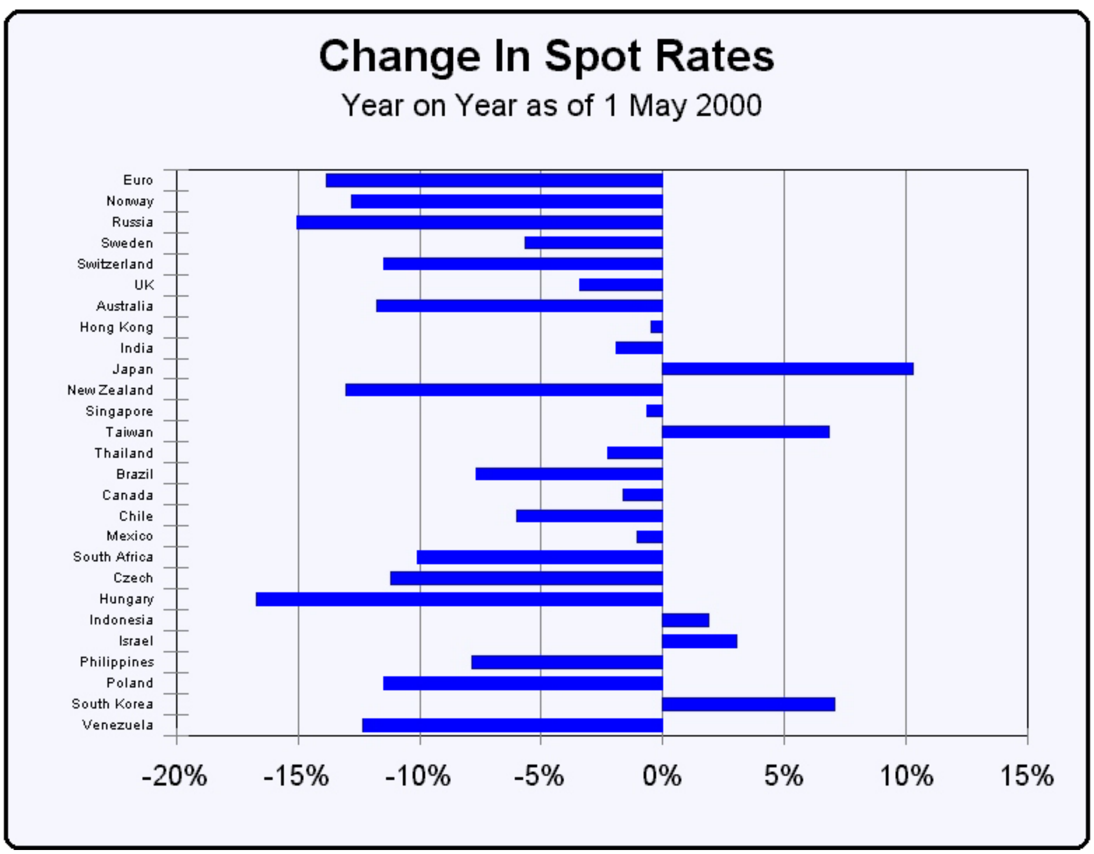
Note that the changes shown here are for spot rates only. If financing costs are taken into account, the results, for the most part, would be worse. The spot rate for the yen, for example, has fallen by nearly 6% so far this year, but if you take into account that interest rates in the US are nearly 6% higher than in Japan, owning yen deposits would have produced an opportunity cost of an additional 2% or so for dollar-based investors. Similarly, the euro has declined not quite 10% so far in 2000, but if financing costs are taken into consideration, euro holdings have lost nearly 11% in dollar terms.

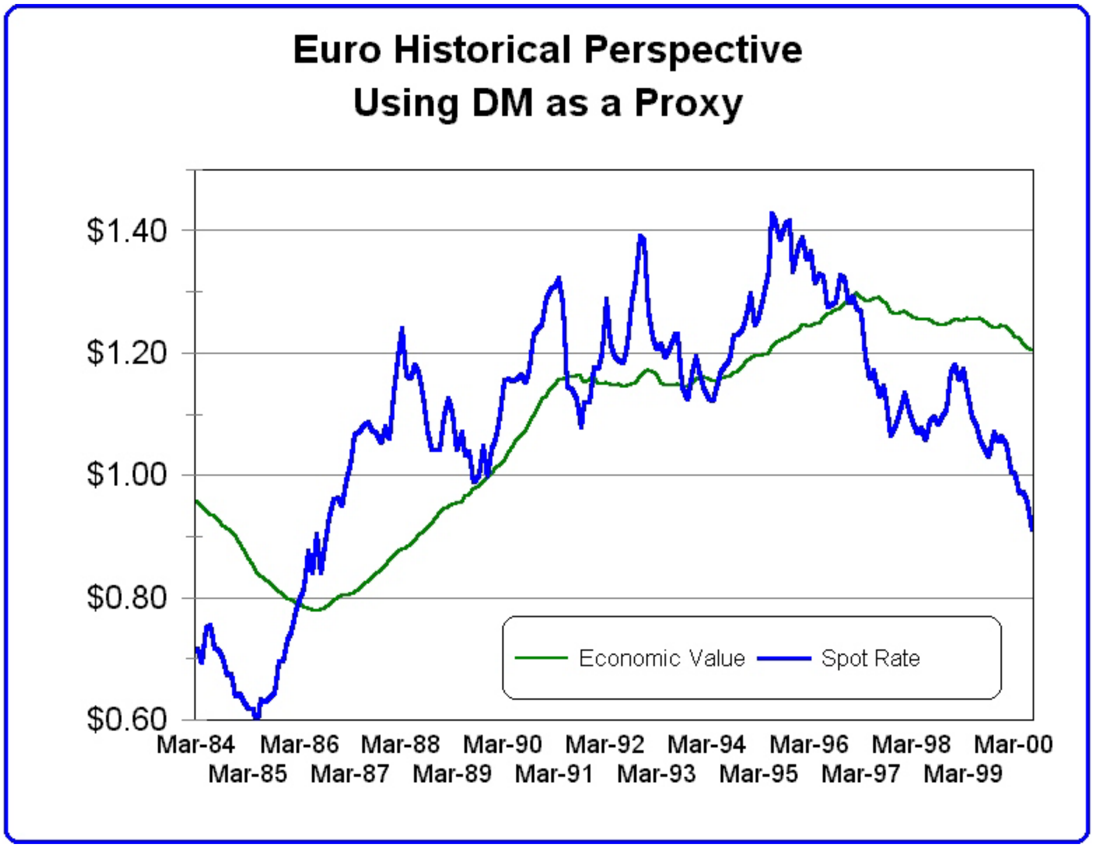
Note that, for the most part, the only currencies to escape the greenback steamroller have been those in smaller markets, mostly in Asia. Of the 28 currencies shown here, only 6 have advanced against the buck thus far in 2000.

A Slightly Longer View

Our second bar chart, at the bottom of this page, provides the perspective of a full year, looking back to the beginning of May 1999. Please note that the scale is different, so the changes don't look as extreme at first glance, but in fact the variation is wider in the second chart than in the first. Still, if you compare the numbers for most currencies, you will see that they aren't all that much different, suggesting that most of the damage of the past year has been done in the last 4 months. The major exception here is the yen, which is actually up 10%+ since a year ago. Only 4 other currencies, all from emerging markets, are ahead of the dollar in this view.

Minor note: there are only 27 currencies in this second chart — we removed the Turkish lira because it distorted the scale too much, being down more than twice the amount of the next worse performer. The fact that the lira has declined in line with the other European currencies so far this year may be a sign that the IMF-sanctioned program to contain inflation in Turkey is having some effect.





A Still Longer View

On this page, we provide an updated version of a graph we have used on previous occasions. As the euro plummets down through 90¢, we all hear talk about it being at an all-time low, but this begs the question of how far one would have to look back to see a similar level if using the deutschemark as a proxy for the euro's historical performance. The answer, as this graphic should make clear, is that the euro (so defined) last was at this level in mid-1986.

But hang on to your hat! A year before that, it had been at (the equivalent of) 60¢! We're not predicting a repeat performance of the dollar's 1985 romp, but it might be well to keep in mind that it has happened before. A more likely scenario, in our view, is that the euro will stop declining sometime later this year, begin to recover, and end up a year from now at a higher level than where it is today. Meanwhile, our short-term outlook remains negative.

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