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In the last issue of the Fortnighter, I mentioned the significant gains that many Canadian investors have experienced over the past few years – as long as they had a healthy amount of U.S. dollar exposure in their portfolios.

It almost didn't matter what an investor purchased in the U.S. – as long as they were there for the big move in the currency, they benefited handsomely. And it wasn't that the Canadian dollar "fell" against the Greenback. Our dollar, in fact, did just fine against other major currencies such as the Yen or Euro. It's that the U.S. dollar was strong against just about everything else.

The surge in the US currency over the past few years highlights the importance of having a "top down" (or "big-picture") view when managing investment portfolios – especially Canadian investment portfolios.

It may be my bias, but I believe the traditional approach of simply picking "good" stocks and holding on to them in an effort to achieve superior investment returns is becoming less and less valid. Understanding the difference between, say, a Suncor and a Canadian Natural Resources is not as important to your rate-of-return as the direction of oil prices or the economy. If oil prices decline by 50%, both companies are likely getting clobbered (and vice versa). Similarly, if interest rates go up dramatically, any Canadian utility stock (such as a Fortis or an Emera) is likely to be similarly impacted. The big picture is important.

The problem is that predicting interest rates, currencies or energy prices (no one saw that coming!) is a lot more complex than saying "I understand company X, they have great management, it's a good business, etc., etc.". But as an investor, it's vital to have an understanding of the framework that your companies (stocks) operate in. So, let's consider the US\$ again.

Until fairly recently, the US currency was not the place to be. The Fed was cutting rates to bring the economy out of recession and commodity-linked currencies (like the Aussie or Cdn\$) appeared more attractive. I regularly had clients tell me that they wanted NO U.S. exposure in their portfolio.

But while all this was going on, countries around the world were borrowing TRILLIONS of dollars in low-rate, US\$ denominated debt – believing they'd be paying back that debt back in the future in cheap dollars. Meanwhile, the US economy was recovering. So now, not only do we have the US\$ rising because the Fed is raising rates and the markets are strong, all these countries now must BUY US dollars so that they can pay back the interest and/or principal on the bonds they issued.

Couple this with the fact that the two other largest economies in the world (Japan and the European Union) are now cutting rates to try and jumpstart growth and things will likely continue to bode well for the US currency. I, for one, will be maintaining a healthy US\$ weight in portfolios.



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