Currency Hedged Indexes: Why Do They Matter?

- Currency exposure has substantially impacted the performance and the volatility of global equity indexes at times—both positively and negatively
- While there are periods in the investment cycle when investors may be comfortable taking on both equity *and* currency risk, there are other times when decoupling the two can be desirable
- MSCI has developed a range of hedging and currency indexes that reflect various ways to capture and/or hedge currency risk in an equity opportunity set. Hedging currency exposure allows an investor to take currency risk out of the equation when investing in companies abroad.

The Importance of Currency Risk

- Currency returns, which reflect changes in exchange rates, can fluctuate considerably
- The US dollar, for example, has gone through multi-year periods of appreciation and depreciation relative to other major developed market currencies like the Euro and the Yen over the past few decades
- The effects of currency exposure on an international equity portfolio's returns and risk have been sizable at times

Effects of Hedging Currency Risk in the Past Year: Examples

- Over the past year (since September 2013), many major currencies have depreciated relative to the US dollar (USD)
- As the US dollar has strengthened over this period, hedging exposure to foreign currencies has benefited US investors holding stocks of foreign companies
- The MSCI Japan Index expressed in USD, for example, earned annualized returns of 0.62% from Sept 2013 to Sept 2014. If its currency exposures had been hedged, the index would have returned 11.90%
- On the other hand, because the USD lost ground to the Euro over the same period, the MSCI UK Index expressed in USD returned 6.12%, outperforming the MSCI UK Hedged to USD Index which returned 5.86%

Performance Characteristics of Unhedged & Hedged MSCI Indexes (USD)—(Sept 2013 – Sept 2014)

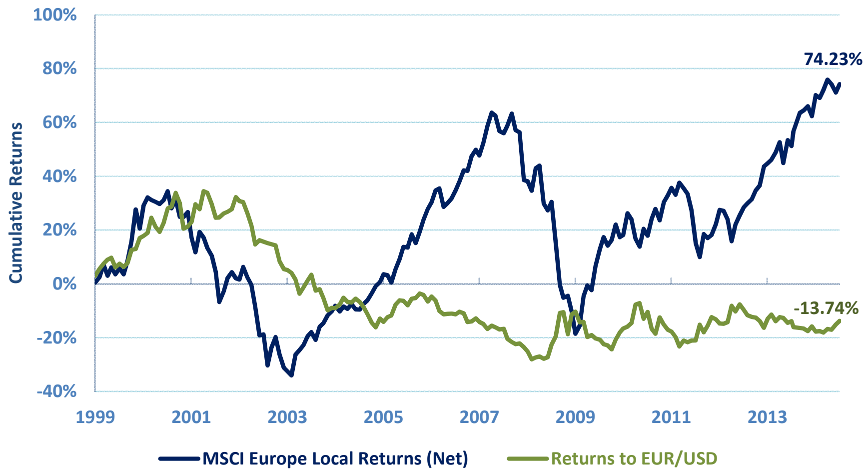
	Unhedged Index	Hedged Index
Annualized Returns		
MSCI EAFE	4.25%	10.50%
MSCI Emerging Markets	4.30%	5.12%
MSCI Brazil	-4.65%	-3.54%
MSCI Germany	1.94%	9.57%
MSCI Japan	0.62%	11.90%
MSCI UK	6.12%	5.86%
MSCI Europe	5.82%	10.98%
MSCI AC Asia Pacific ex Japan	5.96%	6.50%
MSCI Korea 25-50	0.74%	-3.04%
MSCI Mexico IMI 25-50	9.32%	8.54%
MSCI ACWI ex USA	4.77%	9.96%
Annualized Volatility		
MSCI EAFE	9.58%	6.55%
MSCI Emerging Markets	13.67%	9.44%
MSCI Brazil	31.15%	21.27%
MSCI Germany	14.52%	10.24%
MSCI Japan	9.08%	13.00%
MSCI UK	12.59%	9.91%
MSCI Europe	11.74%	7.82%
MSCI AC Asia Pacific ex Japan	12.80%	9.28%
MSCI Korea 25-50	12.54%	9.03%
MSCI Mexico IMI 25-50	13.06%	10.48%
MSCI ACWI ex USA	9.97%	6.43%

Past performance is no guarantee of future results. Index returns assume reinvestment of all dividends. It is not possible to invest in an index.

Why Hedge Currency Risk?

- Currency moves can be quite substantial depending on the time period
- From peak to trough *(May 2007 to Feb 2009)*, the EUR/USD exchange rate lost nearly 50% of its value *(See chart.)*
- Currency losses can be large in magnitude when compared to equity market returns
- In the short run, currency returns can be driven by an array of factors, including Central Bank decisions, changes in inflation, the balance of trade and cross-country capital flows
- Hedging currency exposure is an option for investors in foreign equities who do not want to be exposed to currency fluctuations

***Comparison of the MSCI Europe Index Returns in Local Currency versus the EUR/USD Currency** (Jan 99 – Sept 14)*



Past performance is no guarantee of future results.

MSCI Currency Hedged Indexes

- MSCI has constructed hedged versions of a range of its market cap weighted indexes including base currencies such as the USD, EUR, GBP, JPY, and AUD
- MSCI Hedged Indexes represent a close estimation of the return that can be achieved by hedging the currency exposures of the parent index by selling foreign currency forwards at one-month forward rates
- The MSCI Hedged Indexes weight each currency in correspondence to the relative market cap weight of the securities quoted in that currency in the underlying MSCI parent index

Learn more: MSCI Currency Hedged Indexes

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R-31578-1 (10/14) MSCI Currency

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