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*If you can put the word markets after it, I cover it.*

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# How Emerging Market Mayhem Turns Up In Corporate America's Earnings

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*This is a guest post by Wolfgang Koester, chief executive and co-founder FiREapps, a provider of currency exposure management tools.*

There was a time when only currency traders cared about currency moves. Those days are long over. The panic over massive devaluation of emerging market currencies is a reflection of a new normal for multinational corporations and investors. There is a new normal at play: big currency moves from many different countries at once that are impossible to predict. As headlines around the world exclaimed in January and February, emerging market currencies have dealt significant negative impacts to multinational corporations over the last year.

The currency moves in the latter half of 2013 and early 2014 are now showing up on the balance sheets and income statements of corporates around the world. They led to a reshuffling of the “usual suspect” currencies that corporates typically report as impacting earnings. Those impacts were to the tune of 3 cents per share — three times the increasingly accepted standard of a penny per share — and they led analysts to begin asking more, increasingly pointed and sophisticated questions during earnings calls.

## The Changing Complexion of Impactful Currencies

Since 2012, the “currency culprits” — currencies that corporates mention most often as impacting earnings — have changed. Where it was moves by the euro and the yen that most often affected companies’ revenues in 2012, it was emerging market currencies in 2013:









































- In the first quarter, after a 32% devaluation, the Venezuelan bolivar was the second-most mentioned currency by corporates during earnings calls;
- The Brazilian real was the top most cited currency in the last two quarters, when it declined as much as 21%;
- The Indian rupee showed up on the currency culprits list in the third

quarter, as it declined as much as 14%;

- The Argentine peso made the list in the fourth quarter, when it declined 11%.

At the same time, corporates were reporting impacts from the euro to a lesser and lesser extent; in the last quarter of 2013, the euro was not on the list at all.

**FIREAPPS' Currency Culprits – The 5 Currencies Most Mentioned in Earnings Calls as Impactful (# Companies Mentioning)**

Q1 2012	Q2 2012	Q3 2012	Q4 2012	Q1 2013	Q2 2013	Q3 2013	Q4 2013
EUR (62) 	EUR (138) 	EUR (53) 	EUR (49) 	JPY (89) 	JPY (84) 	BRL (21) 	BRL (14) 
JPY (12) 	BRL (36) 	BRL (13) 	JPY (43) 	VEF (28) 	EUR (30) 	JPY (19) 	CAD (14) 
BRL (12) 	GBP (15) 	INR (8) 	VEF (17) 	EUR (25) 	AUD (28) 	AUD (13) 	JPY (13) 
GBP (10) 	JPY (12) 	JPY (7) 	BRL (10) 	BRL (16) 	BRL (28) 	EUR (13) 	AUD (9) 
MXN (6) 	INR (11) 	CAD (6) 	GBP (6) 	GBP (10) 	VEF (20) 	INR (10) 	ARS (8) 

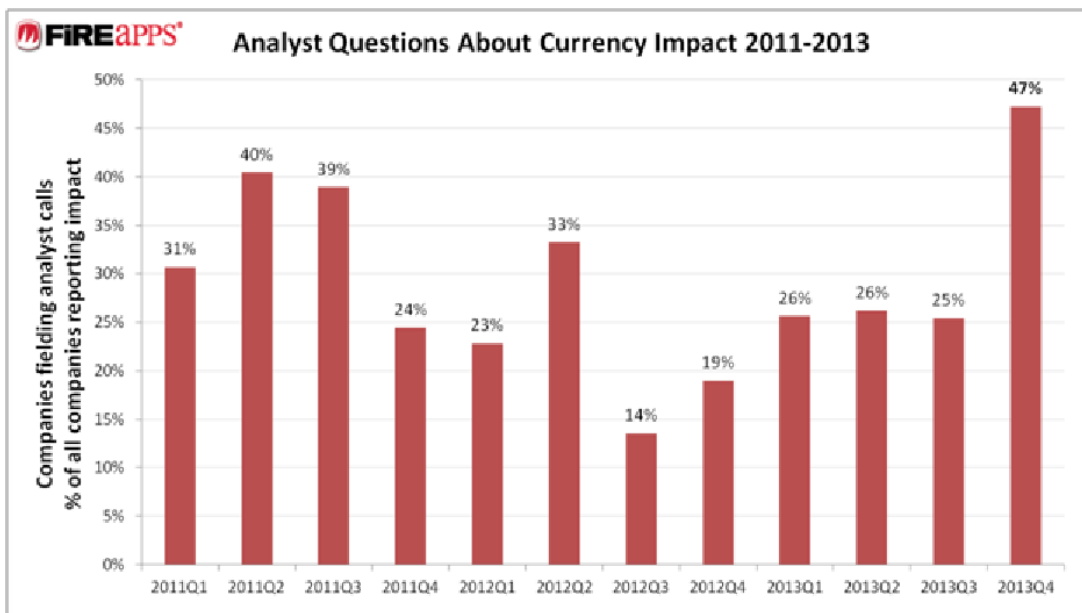
### Surprise Currency Impacts to Earnings per Share

In 2013, the total negative currency impact quantified by corporates in their earnings calls was \$17.8 billion.[1] That currency impact ultimately flows down to earnings per share (EPS) and – as a consequence – affects shareholder value. Within that context, it becomes clear how important currency risk management is; risking EPS is dangerous business because investors tend to react (usually negatively) first and ask questions later on earnings surprises.

FX managers from leading multinationals increasingly have management objectives of less than 1 cent EPS impact. Yet the average EPS impact reported by corporates in 2013 was three times that.

### Increasingly Pointed and Sophisticated Analyst Questions

Given that companies have for three years in a row seen significant negative impacts to EPS from currency volatility, and given the fact that those currency surprises are coming from a growing list of countries around the world, it makes sense that analysts are beginning to ask increasingly pointed and sophisticated questions of CFOs and CEOs during corporate earnings calls.



**Consider, for example, the following exchanges between analysts and CEOs/CFOs.** The three companies highlighted here are not unique, but representative of the general tenor of interaction between analysts and CEOs/CFOs during fourth quarter 2013 earnings calls.

## Colgate-Palmolive

“ *Constance Marie Maneaty – BMO Capital Markets U.S.*

Are there people that you consult about this [foreign exchange]? I’m just wondering if this is a media construct or if it’s something you’re seriously dealing with.

*Ian M. Cook – Chairman, Chief Executive Officer and President, Colgate-Palmolive*

My experience over the last 5 years with foreign exchange is that everybody knows after the fact.

## Avon Products

“ *William Schmitz – Deutsche Bank AG, Research Division*

I know you don’t want to give guidance for the full year, but can you just take a stab at what you think the currency impact is going to be, both in the top line and the bottom line?

*Kimberly A. Ross – Chief Financial Officer and Executive Vice President*

I’m not really going to speculate on that. I mean, if I could predict currencies, I probably wouldn’t be doing this today. So yes, but what I will say is we do expect to have some volatility coming through there. Obviously, Venezuela is also a question mark, as well as some of the other markets. What we’re doing is trying to find ways to mitigate the impact where possible, looking at natural hedges. And we expect that we will have some impact along the way.

## Whirlpool

“ **Kenneth R. Zener** – *KeyBanc Capital Markets Inc., Research Division*

If Latin America volume is flat in '14, could you describe the currency headwind you would expect at today's rates, given the volatility we've seen week to week? We can see the fourth quarter currency hit, but could you kind of frame out, given that there's 35 different countries passing through in America, what it would look like in terms of currency headwind, so we can understand that?

**Larry M. Venturelli** – *Chief Financial Officer and Executive Vice President*

Let me give you a couple of comments. First, for the total year of '13, we absorbed – effectively absorbed about \$85 million of currency headwinds, a lot of that occurring in the second half of the year. And I'm talking in globally. For 2014, we'd expect total currency to be a headwind of around \$50 million based on where currencies are today. The majority of that, a lot of percentage that happen in emerging markets, but we will continue effectively navigate through currency headwinds just as we have over the last couple of years.

[Based on outstanding shares, the currency headwind Whirlpool reported equates to about \$1.51 estimated EPS impact – a huge number, especially given the increasingly common management objective of less than \$.01 EPS impact.]

## **How to Think About the Impact of Currency Volatility on Earnings**

For investors in U.S. corporations, it is critical to understand that some companies' earnings per share are being diminished by currency-related losses. While expansion into emerging markets does indeed hold the potential for significant value returns, that is only the case if the corporation can mitigate the risk associated with doing business in those markets – including the risk of currency impact. To understand how a company is impacted by currencies investors should 1) read Item 3 in the quarterly report; 2) read Item 7A in the annual report; and 3) read the transcript of the quarterly earnings call, which can quickly be searched for key words like “currency” and “foreign.”

*Wolfgang Koester is the CEO and co-founder of [FiREapps](#), provider of foreign exchange exposure management solutions that aim to eliminate surprise currency impacts, reduce transaction costs and increase efficiency. Additional research on emerging market currencies and the earnings impact can be found [on the firm's website](#).*

**[1]** Not all corporates that faced currency headwinds report them in earnings calls. Even among those corporates that do report headwinds, not all of them actually quantify the impact of those headwinds. Still, the quantified impact of currency volatility on multinational corporates has been quite significant.