

How Foreign Forces Affect Your Funds

Which overseas events have the greatest impact on the funds in your retirement account? That depends on the individual fund and the types of assets it holds in its portfolio. Here's what to watch for in five different domestic fund categories:

Domestic stock funds Fluctuations in the value of the U.S. dollar vs. foreign currencies can have an impact on the performance of some funds that own U.S. stocks. The reason: Many U.S. companies earn significant profits overseas, and those profits come in the form of foreign currencies such as the British pound or the Japanese yen.

Say the pound loses value compared with the dollar. Then a U.S. company's profit from sales in the United Kingdom (which comes in the form of pounds) is worth fewer American dollars. As a result, the firm's stock price is likely to fall.

Bond funds typically benefit when U.S. interest rates decline and suffer when rates rise. Thus, they are influenced by overseas factors that affect U.S. interest rates. For example, say European or Japanese bond yields (the interest bonds pay to investors) rise sharply. In that case, companies or government agencies that issue bonds in the U.S. must increase their interest rates to compete for investors. Result: U.S. interest rates rise, and bond prices fall, reducing your bond fund's returns.

Balanced funds typically hold roughly 60% of their assets in stocks. That means they are subject to the effects of foreign currency fluctuations that influence U.S. company profits. But since balanced funds also hold bonds, their performance is also affected by foreign interest-rate moves that affect the U.S. bond market.

Guaranteed Investment Contracts (GICs). These funds buy contracts with insurance companies which in turn invest the money. Since the contracts pay a guaranteed rate of interest for a set period (usually one to five years), and since they are invested primarily in domestic stocks and bonds, their returns are affected only negligibly by international events.

Money-market funds invest in very short-term securities whose prices are supposed to remain stable. However, the income you receive from a money-market fund can rise or fall with changes in U.S. interest rates which might be influenced by rising or falling interest rates overseas.

Investments in money-market funds are neither insured nor guaranteed by the U.S. Government and there is no assurance that they will be able to maintain a stable net asset value.

Say yields on short-term securities rise overseas. U.S. issuers might increase their rates to attract global investors, and your money fund might earn a higher yield. Likewise, if rates on short-term foreign securities decline, U.S. issuers might be able to reduce their rates as well, resulting in a lower yield from your money fund.

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