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U.S. Businesses Worry Stronger Dollar May Weigh on Growth and Exports

Fed officials cite improving U.S. economy as they raise rates, but some don't see it

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American businesses fretted that the first interest rate increase in seven years came at a time when a strong U.S. dollar is already sapping demand for exports and low energy and commodity prices are weighing on growth in the industrial economy.

The Federal Reserve's move Wednesday to raise short-term rates by a quarter percentage point was hardly a surprise to U.S. executives, but it hits as industrial manufacturers like 3M Co. and Honeywell International Inc. offer cautious sales forecasts, as agriculture commodities are in their third year of declining prices, as transportation firms contend with sagging freight volumes, and as food and beverage companies struggle with the strong dollar sapping sales growth.

In making its move to raise rates, the Fed pointed to a strengthening U.S. labor market, stronger household spending and increasing business investment while noting that exports have been soft. The Fed officials said they expect more gradual rate increases in the coming years.

That assessment didn't jibe with what some businesses are seeing. "We're worried because we're seeing leading indicators showing the economy is not in great shape," said Glenn Riggs, senior vice president at Odyssey Logistics & Transportation, which books freight transportation for businesses and operates a fleet of about 300 trucks. "If they raise interest rates and things further slow down, that would be a bigger worry."

Freight volumes sagged this fall, as manufacturing activity slowed and retailers cut back on imports. Mr. Riggs said further interest rate increases could also increase the cost of borrowing to upgrade trucking fleet.

Major businesses from AT&T Inc. to Johnson & Johnson to International Flavors & Fragrances Inc. downplayed the immediate impact of Wednesday's rate increase on business prospects. Longer term, however, further interest rate increases could add to businesses' borrowing costs, cool capital spending, and prompt a reassessment of inventory levels.

The interest rate increase, which the Federal Reserve hopes will spur inflation, is strange for energy companies which are aggressively cutting costs, said Ryan Lance, chief executive of ConocoPhillips.

In "our business that's a concept that is completely out of the radar screen right now," he told an audience in New York at the Council on Foreign Relations.

U.S. oil producers have been pushing their service providers to drop the cost of everything needed in the oil patch, leading to huge deflation in the energy industry, Mr. Lance said.

"I review every week what our deflation capture numbers are," he said. "How much are our service costs coming down?"

Jane Morreau, chief financial officer at Jack Daniel's maker Brown-Forman Corp. said the real effect will be further strengthening the U.S. dollar—an issue that is already weighing on results at beverage alcohol companies. Earlier this month, Brown-Forman said it expects weakening foreign currencies in markets like Russia and Australia to negatively affect results by 5 cents per share during its current fiscal year.

But Ms. Morreau said she trusts that the rate increase signals "an improving U.S. economy, which could benefit our business." The U.S. accounts for about 40% of the company's sales.

Still, many companies have been citing weak economic growth around the globe. Honeywell forecast sales growth in its core businesses excluding acquisitions of just 1% to 2% next year largely due to the troubles in the oil and gas sector. "We're exiting 2015 at a slower growth rates than we had anticipated at this time last year," Chief Financial Officer Tom Szlosek said Wednesday before the Fed's announcement.

Harold Friedman, a vice president at Data2Logistics, a Fort Myers, Fla., processor of freight payments, said the movement of business by the company's retailing and manufacturers suggests the economy "is in a very fragile situation."

"The sheer volume of transactions that we are seeing with our customers is not suggesting there is year-over-year growth beyond 1% or 2%," Mr. Friedman said.

U.S. farmers already struggling with lower prices of major crops like corn and soybeans for the third straight year could be further hurt. Rising global crop stockpiles and the strengthening U.S. dollar have weighed on U.S. grain exports, and a string of benchmark rate increases at a time when central bankers in Japan and Europe are easing monetary policy would further fuel the dollar's rise, analysts said.

"If we see a rate increase, it just reinforces the economic health of the U.S. and reinforces the backing of a strong dollar, which is overall a negative for the farm segment," said Joe Lardy, research manager for the brokerage unit of CHS Inc., the biggest U.S. farm cooperative.

Retail-level farm equipment dealers will face higher interest expenses for holding new and used inventory at their dealerships. Dealers typically borrow money from equipment manufacturers, such as Deere & Co., to purchase new models or acquire used equipment from customers through trade-ins.

"We've got a lot of used inventory. But a small increase in rates won't make much difference" for borrowing costs, said Tom Sloan, CEO of Sloan Implement Co., a Deere dealership with branches in Illinois and Wisconsin.

Ron DeFeo, executive chairman of Terex Corp., a maker of cranes and other heavy machinery, said the Fed's move was positive in that it "takes some uncertainty away."

For now, weak commodity and oil prices have plunged parts of industry into "recession-like conditions," Mr. DeFeo said, but consumers are doing better and their spending eventually should boost manufacturing.

Rising interest rates "reflect confidence in the strength of the economy, and it will eventually work its way into the industrial sector," Mr. DeFeo said.

Meanwhile, rising rates may limit the ability of major chain restaurants from McDonald's Corp. to Wendy's Co. to fund new-store openings and remodeling projects. The burden of such investments falls largely on franchisees, who are taking ownership of an increasing amount of major chain restaurants and have already taken on high levels of debt in recent years to fund such moves.

Small businesses are braced for increases in borrowing costs and further pressure from their bigger customers. "Larger companies that are our customers will typically take longer to pay their bills, which impacts my ability to spend money judiciously on hiring," and other expenses, said Tejune Kang, chief executive of 6D Global Technologies, Inc., a New York-based provider of digital marketing for large corporate clients.

Not all of the impact of the rate increase will be negative for businesses, however.

Verizon Communications Inc. Chief Financial Officer Fran Shammosaid in an interview in September that rising interesting rates would help the company manage its roughly $30 billion unfunded pension and other liabilities by improving the funding level. That could help the carrier improve its bond rating, Mr. Shammo said.

General Motors said the Fed's decision reflects the strength in the U.S. economy that the auto industry has been experiencing. "Auto sales are at a new peak," a GM spokesman said. "We don't expect the rate hike to have any measurable impact on new vehicles sales given the underlying strength of the U.S. economy."

Jeremy Brandt, chief executive of Dallas-based WeBuyHouses.com, says that in the short-term rising rates could spur prospective home buyers to take the plunge.

"Individuals will feel that the gravy train is almost over," said Mr. Brandt, whose company provides services to residential real-estate investors that buy properties to fix them up for resale.

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