Written by **Bob Adelmann** on January 14, 2010

Weak Dollar Obama's Fault?

According to Newsweek, the dollar isn't weakening, and even if it is, it isn't Obama's fault. On Tuesday, Daniel Gross iterated all the reasons that, according to conservatives, the American dollar should weaken. Conservatives, he said, blame the actions of the Federal Reserve with the lowering of interest rates to zero, printing money, and expanding the monetary base. They also blame the Obama administration for running up huge deficits in its efforts to restart the faltering economy.

Gross said, "Let's examine the evidence." He refers to an article in *Conservative Daily News* which suggests it would be in the best interest of the current administration to push for a weaker dollar as it would tend to make American made goods appear cheaper, and as a result would stimulate American exports to foreign countries.

He then tags an article at Bloomberg.com where Harvard professor Niall Ferguson predicted that the dollar "will extend its drop versus the euro over the next two to five years, falling as much as 20 percent to an all-time low under a widening U.S. budget deficit."

To support his claim that the dollar remains stable, Gross refers to a long term chart of the "trade-weighted dollar" index which shows, indeed, that the dollar has strengthened recently against the basket of currencies that make up the index. He also refers to other charts comparing the purchasing power of the dollar to the Japanese yen, the Chinese yuan, the Canadian dollar, the British pound, the Mexican peso, and the South Korean won.

He leaves us with this conclusion:

> If you believe the economic recovery is picking up steam; that the economy may grow at a rate between 3 percent and 4 percent in 2010 (as of Friday, Macroeconomic Advisers said fourth-quarter GDP was tracking at a 5.4 percent annual rate); that the United States will grow more rapidly than the United Kingdom, the Eurozone, and Japan; and that inflation, which has risen just 1.8 percent in the past twelve months, will remain under control, then the greenback's prospects look more rosy.

Those are a lot of BIG "ifs."

The BMOC (Big Man on Campus) of Keynesians, Paul Krugman, said this about the prospects for a stable dollar:

> My prediction is that politicians will eventually be tempted to resolve the [fiscal] crisis the way irresponsible governments usually do: by printing money, both to pay current bills and to inflate

> away debt. And as that temptation becomes obvious, interest rates will soar.

Niall Ferguson, in the near term, doesn't see any significant weakening of the dollar: "From where I am sitting, inflation is a pretty remote prospect. With U.S. unemployment above 10 percent, labor unions relatively weak, and huge quantities of unused capacity in global manufacturing, there are none of the pressures that made for stagflation (low growth plus high prices) in the 1970s. Public expectations of inflation are also very stable, as far as can be judged from poll data and the difference between the yields on regular and inflation-protected bonds."

However, Ferguson is much less sanguine over the longer term. He points out that the deficit for fiscal year 2009 was "a bigger deficit than seen in the past 60 years — only slightly larger in relative terms than the deficit in 1942. We are, it seems, having the fiscal policy of a world war [but] without the war." He says that "unless entitlements are cut or taxes are raised, there will never be another balanced budget." He does point out that there is a third option: "a significant dollar depreciation seems more probable, since the United States is in the lucky position of being able to borrow its own currency, which it reserves the right to print in any quantity the Federal Reserve chooses."

A careful look at the chart of the trade-weighted dollar reveals the long decline of the dollar since 2002: from 130 to just over 100 currently, a decline of 30 percent in less than 8 years. Another point to keep in mind is that this "basket" of currencies represents other paper currencies that have, in general, been losing value over the same period of time. A reasonable conclusion is that the American dollar is "the best of a bad lot."

A chart of the performance of the dollar versus gold since 2002 reveals a vastly different picture of the dollar's stability with gold moving from $250 an ounce in 2002 to over $1100 an ounce currently. Put another way, $1,000 in 2009 is worth only $187.21 in 1971 dollars (when President Nixon took the U.S. off the international gold standard).

Gross does admit in his *Newsweek* article that "the dollar's recent upturn and relative stability could be a mirage. It's entirely possible that the [American] currency could collapse if inflation surges or economic conditions deteriorate. If you believe the U.S. economy will scrape along bottom for the next few years and that inflation will spike, then prolonged dollar weakness seems likely."

Obama, then, is clearly not at fault for weakness in the dollar, although such weakness might serve his administration well in the short run. Nor is such weakness to be blamed on either of the Bush administrations, the Clinton administration, or the Reagan administration. Ever since 1971, the Federal Reserve alone, with its monopoly on printing currency and creating money out of nothing, has successfully weakened the dollar.

Thomas Jefferson warned us:

> I place economy among the first and most important virtues, and public debt as the greatest of dangers to be feared. To preserve our independence, we must not let our rulers load us with perpetual debt. If we run into such debts, we must be taxed in our meat and drink, in our necessities and in our comforts, in our labor and in our amusements. If we can prevent the government from wasting the labor of the people, under the pretense of caring for them, they will be happy.

I believe that banking institutions are more dangerous to our liberties than standing armies. Already they have raised up a monied aristocracy that has set the government at defiance. The issuing power (of money) should be taken away from the banks and restored to the people to whom it properly belongs.

This warning about banking institutions and their protector, the Federal Reserve System, was implemented in Article I, Section 10 of the Constitution of the United States: "No state shall . . . coin money, . . . or make anything but *gold and silver coin* [emphasis added] a tender in payment of debts . . ."

Gross was partly right: Obama has had little to do with the weakening of the dollar over the years. The “conservatives” he quotes are also right: the dollar will continue to weaken until it is worthless, or until the Federal Reserve System and its printing presses are abolished.