



What's wrong with a weak dollar?

October 2009

While the official US government position regarding the dollar is strength and stability, an unofficial weak dollar policy appears to be the reality. And why not? As our federal debt soars toward record levels not even seen during World War II, weak dollar policy is very tempting. If the Treasury converts short-term debt to long-term debt and the weak dollar trend continues, they can simply devalue their way toward less debt in real dollars terms, and into prosperity. Exports will continue to increase and eventually American workers will become cost competitive in foreign currency terms causing an increase in US manufacturing jobs. Investors have and will continue to benefit from the weak dollar by purchasing commodities, foreign currency and foreign stock. Investors can even lever their returns by borrowing in dollars and investing in these non-dollar assets. If it sounds too good to be true, long-term it is.

The problem is that the weak dollar causes a drain of domestic capital that is the life-blood of domestic jobs. Even though exports increase in a weak dollar environment, the massive exodus of capital causes more job losses than export driven job gains. Job growth is the foundation of economic turnaround and the ultimate source of tax revenues to repay the debt. A weak dollar erodes that foundation.

So why doesn't the US take steps to stabilize the dollar and foster jobs growth? Much of the solution requires an increase in interest rates and fiscal restraint, neither being politically palatable in a fragile and ironically jobless economic recovery. There have been US leaders that have done what is right instead of what is politically expedient, but they are few and far between. Paul Volcker, former Chairman of the Federal Reserve, was one such leader in the 1970s and the current situation begs for that type of leadership. But the reality is that we are in a downward dollar trend.

Eventually world bond markets may force US fiscal restraint and a stable dollar. While globalization has many challenges it may also be creating necessary checks and balances. It may be that China and other large foreign purchasers of US debt ultimately demand sound US fiscal policy, lest they discontinue purchasing our debt. Globalization is the key to world economic recovery and prosperity, and the US needs to be a viable participant through fiscal responsibility.

While it may almost seem unpatriotic to invest in foreign markets and commodities to offset the weakening dollar, that is also the reality of open markets. Investors will always seek the best risk adjusted return available, and US policy will eventually adapt.

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