



advertisement



LINCOLN

Dulaney Lincoln Mercury
Great selection of new and pre-owned vehicles



MERCURY

< CLICK HERE FOR LOW INTERNET PRICES >

<http://www.baltimoresun.com/business/investing/bal-bz.hancock05oct05.1.1277729.column>

Dollar's recent gains shame its worst critics

Jay Hancock

October 5, 2005

Warren Buffett's digestion is threatened these days by more than T-bone steaks and Dairy Queen ice cream. Often as not recently, the world's foremost dollar doubter has been waking up to find the greenback gaining in value, shaming its critics and costing him and his shareholders millions.

The dollar is on the march again after rising sharply this year against the euro, the British pound, the Swiss franc, the Japanese yen and other major currencies.

Who cares?

Berkshire Hathaway shareholders do. Not long after boss Buffett decided he was not just a stock-picker but an applied macroeconomist, competent to bet on global fund flows, Berkshire began lagging behind the stock market. Last month, Berkshire shares hit their lowest point in almost two years, although the drop is partly connected to anticipated costs from hurricane-insurance claims.

But dollar strength matters for everybody else in the economy, too.

If the greenback continues to rise or at least maintains most of its recent gains - and there is no reason why it shouldn't, barring some unforeseen shock - many scary stories you've heard about the future U.S. economy won't come true.

Dollar strength means the Chinese, Indians, Japanese and world's other great savers will continue to finance U.S. consumers with low long-term interest rates.

Dollar strength suggests U.S. housing prices will level off or fall only slightly after their spectacular rise, avoiding the mortgage-rate spike that some believed would cause a crash. Dollar strength means that non-petroleum imports will stay cheap and that the country will avoid a bad inflation problem.

Dollar strength implies continued health in U.S. stock and bond markets and continued cheap access to capital for U.S. companies needing to expand or upgrade. And dollar strength means the United States can afford to keep acting as the global buyer of first and last resort, saving the world from a bad recession and all the accompanying grief and turmoil.

Buffett and the other dollar bears bought into one of the oldest dollar-disaster scenarios in the book. They saw Federal Reserve chief Alan Greenspan pumping up the dollar supply from 2001 to 2004, which naturally was supposed to lower the price.

They saw soaring U.S. consumer debt, government debt and trade deficits, which raised questions about the American

balance sheet and the country's ability to repay. And they figured that at some point central banks and other investors would lose confidence and dump U.S. stocks and bonds, sending the dollar sharply southward.

So far they have been mostly wrong. It's true that Buffett is probably still ahead on his anti-dollar bets, which began in 2002 and involve contracts relating to the dollar's value versus the euro, British pound or other foreign currencies.

But from January through June of this year, Berkshire showed paper losses of nearly \$1 billion on currency bets. The dollar fell a bit over the first part of summer but regained ground in September, so Buffett may show another loss for the third quarter.

On the year, the dollar has risen more than 10 percent against the euro, yen, Swiss franc and other currencies. The euro is close to its 2005 low of \$1.187. Since early September, the dollar has risen 2.6 percent against a basket of currencies issued by U.S. trading partners.

And as Greenspan keeps reversing his former lavishness by raising short-term interest rates and making short-term U.S. paper more attractive, currency geeks are wondering whether Buffett will throw in the towel and cancel his bets by buying dollars, which would propel the greenback even higher.

What happened? For all its flaws, the U.S. economy is still the most dynamic and robust in the world, practically demanding that investors buy dollars and put their money here. The key variable as always is labor productivity - economic output per worker, which is a good long-term predictor of rising corporate profits, worker pay and tax revenue.

Since the mid-1990s, U.S. productivity growth has recovered from its 1970s-1980s slump and furnished the nation with the ability to handle its enormous debts. U.S. productivity growth has exceeded 3 percent the past three years and might do so again this year; Europe's productivity growth rate, on the other hand, sometimes flirts with zero. Where would you put your money?

A strong dollar is not pain-free. It hurts manufacturers and factory workers because it makes imports cheap and exports expensive. And although rising productivity eventually leads to higher worker incomes, this time it's taking a darn long time to do so.

But on the whole, you'd rather have a strong national currency than the opposite. Maybe Buffett should switch back to a pure stock portfolio. Or Maalox.

.....
jay.hancock@baltsun.com

Copyright © 2005, [The Baltimore Sun](#) | [Get Sun home delivery](#)