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Geithner Weak Dollar Seen as U.S. Recovery Route (Update1)
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(Updates with Dollar Index gain in seventh paragraph.)

By Ian Katz and Simon Kennedy

Oct. 19 (Bloomberg) -- For U.S. Treasury Secretary Timothy F. Geithner, a weaker dollar may now be in the national interest.

The dollar has dropped more than 7 percent since Aug. 27, when Chairman Ben S. Bernanke signaled the Federal Reserve is prepared to ease monetary policy. Where once such a decline may have been met with resistance from the U.S., Geithner may now be tolerating it as a way of bolstering the recovery.

Companies from Costco Wholesale Corp. to Deere & Co. have credited the weaker dollar for giving their earnings a boost, and the currency's slide has helped propel the Dow Jones Industrial Average above 11,000 for the first time since May.

Higher stock prices in turn are bolstering consumer and business confidence. The danger is that the decline gets out of hand, fueling increases in the cost of living over the long term and prompting investors to avoid U.S debt.

"In an era where deflation pressures appear to be the greatest risk, growth is below trend and the U.S. wants to boost exports, why would they not want" a weaker dollar, Jim O'Neill, chairman of Goldman Sachs Asset Management in London, said in an interview. "The answer is when it becomes a problem for financial markets. Until then it's a straightforward strategy."

The U.S. currency is slipping in reaction to a decline in interest rates that's making U.S. assets less attractive to overseas investors. The yield on the two-year Treasury note touched 0.3508 percent yesterday, the least since reaching a record low 0.3270 percent on Oct. 12.

Dollar Index

The Dollar Index, used by IntercontinentalExchange Inc. to track the greenback against six currencies including the euro, yen and pound, has dropped about 7 percent since Aug. 27, when Bernanke said the Fed "will do all that it can" to ensure a continuation of the economic recovery.

The index gained 0.4 percent today to 77.275 as of 9:08 a.m. in London. The gauge, which began in 1967, is still close to its low reached in April 2008.

The dollar is trading near parity against its Australian counterpart for the first time since 1983, and is close to its weakest versus the yen in 15 years.

Geithner said yesterday that the U.S. will preserve confidence in a "strong dollar." Speaking at an event in Palo Alto, California, he said the U.S. "will not engage" in currency devaluation.

Weaker Dollar

A weaker dollar can help the economy by making U.S. products less expensive in overseas markets and by boosting the overseas earnings of U.S. companies in dollar terms. As the cost of imports rises, American consumers switch to U.S.-made goods, and domestic producers face less competition from abroad.

"The dollar is going to go down," Martin Feldstein, a Harvard University professor who was chief economic adviser to President Ronald Reagan, said Oct. 7 in a Bloomberg Television interview on "Surveillance Midday" with Tom Keene. "It will cause Americans to shift from imported goods into domestic services. All of that will strengthen the economy."

The trade gap widened 8.8 percent in August to $46.3 billion. Imports from China climbed to a record $35.3 billion in August, pushing the trade shortfall with the Asian nation to $28 billion, the highest since comparable data began in 1992.

The Standard & Poor's 500 Index has jumped 13 percent since Bernanke's speech on prospects that economic growth will be spurred by a resumption of large-scale asset purchases by the Fed and exporters' earnings will benefit from a weaker dollar.

Overseas Sales

Companies in the S&P 500 that get more than half of their revenue internationally have returned about 5.1 percentage points more than those whose sales comes mostly from the U.S. since the start of September, according to data compiled by Bloomberg.

A weaker dollar is "a positive for equities as long as it's not viewed as a collapse of the dollar," said Paul Zemsky, the New York-based head of asset allocation for ING Investment Management, which oversees $550 billion.

Matt McCormick, portfolio manager at Cincinnati-based Bahl & Gaynor Inc., which manages $2.9 billion, said the dollar's weakness is benefiting companies he owns with "significant" overseas revenue, including McDonald's Corp., Procter & Gamble Co., Intel Corp. and Qualcomm Inc.

"A low dollar will be with us for longer than most people expect," he said.

Currency 'Tailwinds'

Issaquah, Washington-based Costco, the largest U.S. warehouse club chain, is benefiting from foreign-exchange "tailwinds," Chief Financial Officer Richard Galanti said Oct. 6. He said the dollar's decline in many of the countries where the company operates increased sales by about $1.6 billion over the course of its fiscal year.

Moline, Illinois-based Deere, the world's largest farm equipment maker, said in August that net sales of worldwide equipment operations rose 6 percent in the nine months ended July 31 from a year earlier, including a favorable currency translation of 3 percent.

Lawson Software Inc., a St. Paul, Minnesota-based provider of business-management software to Safeway Inc. and the Mayo Clinic, said appreciation of the euro on the quarter ended Aug. 31 boosted sales above its projections.

The economic benefits of a weaker currency give Geithner reason to downplay the "strong dollar" policy first articulated in about 1995, when he was deputy assistant Treasury secretary under Robert Rubin, who served as the Treasury secretary from 1995 to 1999.

‘Free Market’

“Geithner’s comments recently have been not exactly dollar-supportive,” said Barry Knapp, chief U.S. equity strategist at Barclays Plc in New York. “Typically what happens is that the Treasury either says we support a strong dollar or we think a free market should decide where the dollar goes, and that means we don’t mind if it goes down.”

That doesn’t mean the administration is actively trying to drive down the currency, which investors might interpret as a U.S. effort to devalue its way out of debt, said Jacob Funk Kirkegaard, a senior fellow at the Peterson Institute for International Economics in Washington.

Even if the U.S. is not trying to push the dollar higher, “you can’t say that that amounts to having an active policy to drive down the dollar,” he said.

Geithner this month blamed China’s policy of limiting gains in the yuan for contributing to a “damaging dynamic” of capital controls and currency-market interventions by emerging economies.

“It is very important to see more progress by the major emerging economies to more flexible, more market-oriented exchange-rate systems,” he said Oct. 6.

‘Significantly Undervalued’

Geithner went further in comments yesterday, saying the yuan is “significantly undervalued, more so than is true of any major, significant emerging-market currency.”

A weaker dollar may be a relief for the U.S. economy, with an unemployment rate that is forecast to exceed 9 percent through next year, according to the median estimate in a Bloomberg News survey of economists.

In his State of the Union address in January, President Barack Obama said U.S. jobs will depend in part on the country’s ability to boost overseas sales. Meeting his target would mean exports reaching $3.14 trillion by 2015 from $1.57 trillion in 2009, according to the White House.

As long as the decline is “orderly, not negatively impacting U.S. asset prices -- Geithner is quite happy with the depreciation in the currency,” said David Gilmore, a partner at Foreign Exchange Analytics in Essex, Connecticut.

Yuan Gains

Still, developing nations may not cooperate as they seek to protect their own exports and curb inflows of capital that threaten to lift their currencies.

China, the second-largest trading partner for the U.S. after Canada, has limited gains in the yuan to 2.7 percent since it dropped its peg to the dollar in June.

“We are committed to a more flexible exchange regime,” Yi Gang, Deputy Governor of the People’s Bank of China, said on Oct. 9 during a meeting of the International Monetary Fund in Washington. “But the approach is probably a gradual one.”

Brazilian Finance Minister Guido Mantega, who has spoken of a "currency war," yesterday said the country will increase a tax on foreigners' investments in fixed-income securities to 6 percent from 4 percent. The tax on foreign investors' margin deposits for futures markets will climb to 6 percent from 0.38 percent, Mantega told reporters in Sao Paulo.

G-20 Frictions

India's central bank may intervene in currency markets if the rupee appreciates past 43 against the dollar, a finance ministry official with knowledge of the matter said Oct. 18. The rupee has climbed 3.3 percent in the last month to 44.36 per dollar yesterday.

Frictions may fester this week as Geithner and Bernanke meet with counterparts from the Group of 20 developed and emerging nations Oct. 22-23 in South Korea to craft an agenda for a Seoul summit of leaders next month.

"Each of these central banks and Treasury departments recognizes there is a competitive beggar-thy-neighbor devaluation game going on and that's something you don't want to be left behind in," said Stephen King, chief economist at HSBC Holdings Plc in London.

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