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Opinions

The ‘exorbitant privilege’ and its stubborn costs

By Robert J. Samuelson May 6 at 12:04 PM

It’s been called the “exorbitant privilege”; it might also be termed “the indestructible curse.” Americans are proud of the fact that the dollar — their money — is also the world’s dominant international currency. But this very same global role also helps explain some of Americans’ major complaints about the world economy: why we constantly run sizable trade deficits; and why U.S. manufacturers often are at a price disadvantage with foreign competitors.

It’s not that other currencies (mainly the euro and yen) don’t play a global role. They’re also used to pay for imports and for cross-border borrowing and lending. The dollar simply overshadows them. Dollars constitute 63 percent of countries’ foreign exchange reserves, almost triple the next closest currency, the euro (22 percent), says the International Monetary Fund.

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Partly, the dollar’s role reflects inertia. After World War II, with much of Europe and Asia in ruins, the U.S. currency dominated by default. Later, the dollar benefited from America’s wealth and legal system. The United States is regarded as a safe haven, says economist Eswar Prasad in his book “The Dollar Trap.” Foreigners can invest their dollars in the world’s deepest stock and bond markets. And “the rule of law is firmly established. ... Foreign investors [know] they will be treated fairly if they invest in the U.S.,” he writes.

It was Valery Giscard d’Estaing, French finance minister and later president, who called the dollar’s global role an “exorbitant privilege.” By this, he meant that the United States could pay for imports simply by printing more money. Other countries need to export to earn the foreign exchange (mostly dollars) to pay for imports. There’s a “something for nothing” quality to the dollar’s status that — paradoxically — also fuels discontent with globalization.

What most galls Americans is that other countries, by manipulating their currencies, give their exporters an unfair advantage over U.S. rivals. At various times, China, Japan, South Korea and Taiwan have been accused of currency manipulation. “Our American-made exports are more expensive, while our competitors’ exports into our country are cheaper,” says Sen. Rob Portman (R-Ohio), who wants the Obama administration to negotiate tough prohibitions against manipulation in talks over the Trans-Pacific Partnership (TPP).

There are two problems. The first is that the worst of abuses may be over. Since 2005, China has allowed the yuan to appreciate 33 percent. The Wall Street Journal recently reported that the International Monetary Fund thinks the yuan is “fairly valued.” American officials disagree, but any undervaluation seems to have shrunk. As for the recent depreciations of the yen and the euro, they reflect easy monetary policies by the European Central Bank and the Bank of Japan. Hardly anyone thinks that flexibility can be withdrawn. The last time Japan intervened directly in foreign exchange markets was 2011, reports Portman’s staff.

The second problem is that manipulation is not the only source of pressure on the dollar. The textbook way in which trade deficits are cured is through currency sales and purchases on foreign exchange markets. The country with a deficit sees its currency sold; the resulting depreciation makes its exports cheaper and imports more expensive. The opposite occurs for surplus countries. But for the dollar, this adjustment is incomplete. Global traders, investors and central banks don’t sell all their excess dollars. The result: The dollar remains higher than it otherwise would. The growing demand for dollars for global investment intensifies this upward pressure, as Prasad notes.

Since 1976, the United States has not had one annual trade surplus. It’s hard to believe that all these deficits reflect poor U.S. competitiveness. In reality, our deficits supply the world with a currency to conduct international trade and investment. What’s good for the global economy (and for many Americans, too) is bad for U.S. manufacturers and their workers, whose products suffer a permanent price disadvantage. For them, the global dollar is no privilege. It’s a stubborn curse.

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