dallasnews.com
The Dallas Morning News

Bob McTeer: Pots calling the kettle black

November 10, 2010

I continue to be surprised by how relevant my early schooling remains decades later. If I'd known, I'd have studied more.

My doctoral dissertation was on "Economic Independence and Insulation Through Flexible Exchange Rates," and my first article was on flexible exchange rates. That was in the 1960s, when Milton Friedman was leading the charge for flexible exchange rates as the free-market alternative to exchange-rate pegging or price fixing.

This visit down memory lane was prompted by Tuesday's headline in *The Wall Street Journal* : "Fed Global Backlash Grows; China and Russia Join Germany in Scolding; Obama Defends Move as Pro-Growth."

The move in question, of course, was the Federal Reserve's decision to resume monetary policy easing by purchasing Treasury bonds. That decision was a response to an unemployment rate stuck at 9.6 percent, a recent slowdown in already weak GDP growth, a decline in total employment in three of the past four months, a low and declining inflation rate, weak money growth and fiscal policy off the table over deficit concerns.

If ever there was a time to ease policy to kick-start the economy, that time is now. The Great Depression and the Japanese Deflation remind us of the dangers of timidity and hesitation.

The main argument for flexible exchange rates that led to their widespread adoption in the early 1970s was that they allow domestic policymakers to adopt policies appropriate to domestic conditions without the artificial constraint of an exchange rate peg. The exchange rate adjusts to reconcile the domestic economy and policies with those abroad. The exchange rate adjusts to the economy rather than the economy adjusting to the exchange rate. While the intent of policy easing isn't necessarily to weaken the dollar, a weaker dollar is indicated by our large and persistent trade deficit, particularly with China.

Somehow, the Fed's domestic monetary policy action taken to counter domestic economic ills has been taken by domestic critics and foreign officials alike as competitive dollar devaluation. The *WSJ* article quotes the German finance minister as saying: "It doesn't add up when the Americans accuse the Chinese of currency manipulation and then ... artificially lower the value of the dollar."

Artificially lower the value of the dollar? The Fed is conducting monetary policy to counter high unemployment and possible deflation. It has not intervened in foreign exchange markets to depress the dollar as the Chinese do routinely to depress the yuan. The Chinese are doing the pegging, not us.

In blogs and speeches I've been tolerant of Chinese currency intervention, assuming they will come around when we stop badgering them publicly. That makes it hard to tolerate their lectures accusing us falsely of doing what they are doing.

What to say about the Russian criticism? The Russian G-20 negotiator is quoted by the *WSJ* as saying, "Russia's president will insist 'such actions [as pumping cash into the U.S. economy] are taken with preliminary consultations with other members' of the G-20."

Let me get this straight. Russia, who defaulted on its debt and sent the world into crisis in 1997, now wants a say in internal U.S. monetary policy. I don't know what to say.

How about chutzpah?

Bob McTeer, a distinguished fellow at the National Center for Policy Analysis, is former president of the Federal Reserve Bank of Dallas and chancellor of the Texas A&M University System. His e-mail address is ***bob@bobmcteer.com****.*