Economics

Yellen Ending Trump Dollar Tumult Promises Cheers in Markets

By Liz McCormick and Saleha Mohsin
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- Trump administration often contradicted itself on greenback
- Currency markets welcome stability around strong-dollar policy

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Wall Street Sees 'Easy Money' With Yellen at Treasury: Bianco

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Now that President-elect Joe Biden has picked Janet Yellen as his Treasury secretary, currency markets are growing more confident that the U.S. government's policy for the dollar will be more clear.

Donald Trump's administration conjured chaos about the greenback, one moment threatening to intervene or otherwise fretting about the currency's strength, then -- often on the same day -- taking a contradictory stance. From Bill Clinton's administration through Barack Obama's, the federal government adhered to the position that a strong currency is a reflection of the strength of the U.S. economy.

Prospects that Yellen will returning clarity on dollar policy may help stabilize the $6.6-trillion-a-day currency market that's the backbone of global finance and commerce. Some traders are hopeful even though the former Federal Reserve chair and her new boss, Biden, are expected to take time to unfold their position on the greenback as they focus initially on fighting the pandemic and its economic damage.

"The Yellen appointment may formulate a more coherent policy for the dollar," Ben Emons, head of global macro strategy at Medley Global Advisors, said in a note. "The reason is that during Yellen's tenure as chair, Fed policy uncertainty fueled the strength of the dollar. Her experience and knowledge could see a better, formal setting around dollar policy."

The U.S. Treasury secretary has historically been in charge of the dollar, with a unit in the department dedicated to foreign exchange policy.

But tradition went by the wayside under Trump. The president and his aides freely discussed the currency, often overstepping Treasury Secretary Steven Mnuchin, and the administration overall showed far less commitment to a strong dollar due to Trump's obsession with U.S. trade deficits.

In July 2019, Trump and his top economic adviser, Larry Kudlow, publicly debated a U.S. intervention to weaken the currency after the European Central Bank signaled looser monetary policy, causing the euro to weaken against the greenback. Within hours of each other, Kudlow said in a television interview that the administration had decided not to intervene, only to have Trump tell reporters that the idea was still under consideration.

Former Treasury Secretary Larry Summers says it's time for the U.S. to return to the strong-dollar policy established during the Clinton administration.

"It would be unwise to appear actively devaluationist or indifferent to the dollar," he said earlier this month in an open letter advising the next Treasury chief.

Yellen has in the past noted that a stronger dollar exacerbates the U.S. trade deficit and dampens growth, while a weaker currency does the opposite. She also in 2014 warned her then-Fed colleagues about the risks of commenting on the dollar.

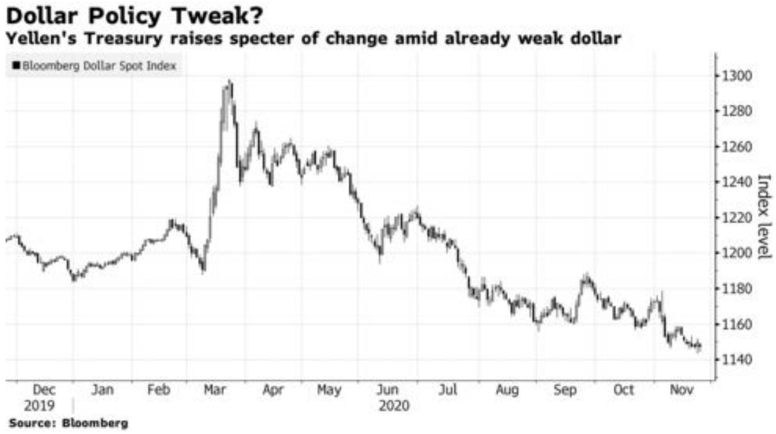
"As a former Fed chair, Yellen also fully understands the impact she could have on markets," Ian Katz, an analyst at Capital Alpha Partners, wrote in a note. "She will choose her words carefully. Investors shouldn't worry that she will make off-the-cuff remarks that will spur volatility."

Any policy changes under Yellen would coincide with growing consensus on Wall Street that the dollar has entered a period of prolonged weakness. A Bloomberg gauge of the greenback's value just hit a 2 1/2-year low.

"Given that we see the dollar falling through Biden's term, the issue of dollar policy could be of some significance," Standard Bank's head of foreign-exchange strategy, Steven Barrow, said in a note. "More than this, the era of almost non-existent foreign-exchange intervention by developed nations could be about to end as well."

The U.S. last intervened in currency markets in 2011, along with international peers, after the yen soared in the wake of that year's devastating earthquake in Japan.

The dollar has fallen more than 11% since March, as measured by the Bloomberg Dollar Spot Index.



Dollar bears have been emboldened by expectations that the Federal Reserve will keep rates near zero for years and that there will be diminished "haven" demand for the dollar given promising results for coronavirus vaccines. That trajectory may continue with Yellen at Treasury, as she's seen pushing to join Fed Chair Jerome Powell's policy of lower-for-longer interest rates with extended, expansionary government spending.

Biden May Get the Weaker Dollar That Eluded Trump's Presidency

Not everyone agrees Yellen will make strong pronouncements on dollar policy, since her focus will be on the domestic economy. Nine months into the pandemic, more than 6 million people still claim extended unemployment assistance and joblessness is again on the rise as U.S. coronavirus infections spike.

"Yellen is unlikely to forcefully articulate a specific policy on the dollar as she no doubt recognizes that domestic policies are far more important to the U.S. recovery and that trying to control or jawbone the exchange rate's value should not be a major priority," said Eswar Prasad, who wrote 'The Dollar Trap: How the US Dollar Tightened Its Grip on Global Finance.'

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– With assistance by Chris Anstey

(Adds analyst comments in 11th paragraph)