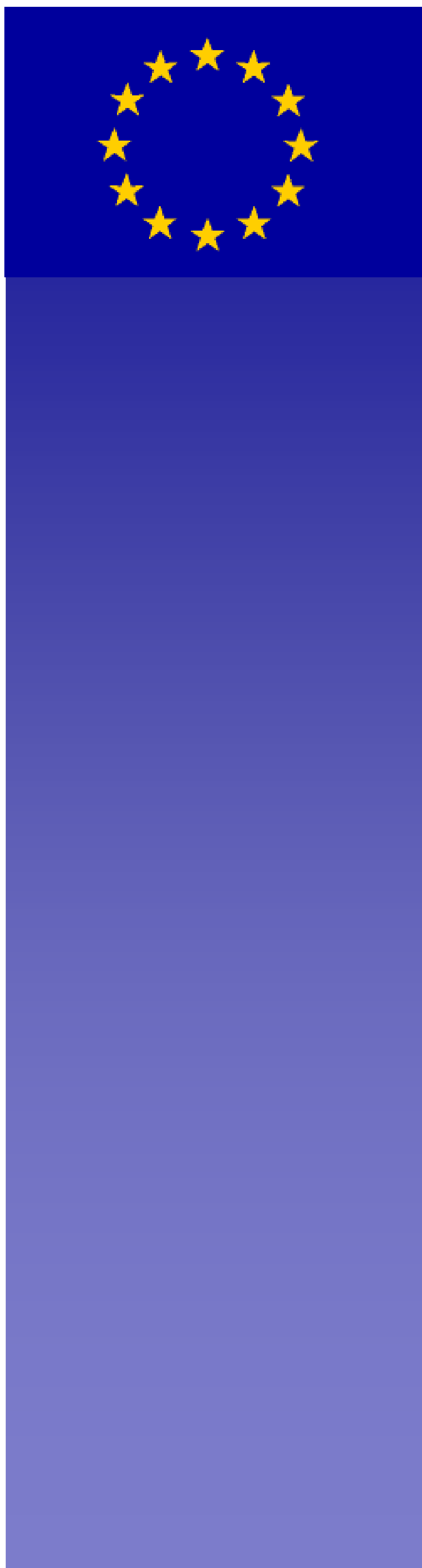

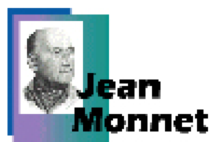

R. Schuman

Miami-Florida European Union Center of Excellence

The US dollar and the euro – *Deus Ex Machina:*

The dollar may be our currency, but it's your problem

Maria Lorca-Susino

Vol.5, No.9
April 2008

Published with the support of the EU Commission.

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The US dollar and the euro - *Deus Ex Machina:*

The dollar may be our currency, but it's your problem.[1]

Maria Lorca♣

Introduction

Until the 19th and mid-20th centuries, economic theory explained that the economic status of a country was represented by the strength of its currency.[2] This strength is measured by the exchange rate of one currency vis-á-vis another currency, a "zero-sum" game in which one currency gains what the other loses. In fact, during the 19th century, the strength of the Pound Sterling facilitated Britain's global hegemonic political and economic power known as the Pax Britanica. During the 20th century, the strength of the US dollar represented both the economic and political hegemony of the US around the world known as the Pax Americana. Nowadays, the weakness of the US dollar is making specialists wonder if we are witnessing the end of Pax Americana and the beginning of something else, possibly a *Pax Europea*, led by the strength of the euro.

This is the argument surrounding the current behaviour of the US$-€exchange rate and its effect on the economic performance of these two economic blocs. While the current exchange rate between the US dollar and the euro has been considered a blessing for the US, it has become a matter of concern for most Eurozone countries. In fact, we are witnessing an unprecedented scenario where the country with a weak currency is actually pleased and the group of countries with a strong currency is worried. The strength of the euro is becoming irritating for the Eurozone and, nevertheless, the weakness of the US dollar is also pushing it to the brink of losing its status as a global currency.

This exchange rate debate is accompanied by another debate concerning how the latest monetary policy actions taken by the US and Eurozone monetary authorities[3], aimed at solving current economic imbalances, are affecting the US$-€ exchange rate. Scholars, economists, and politicians argue that these monetary policies seem unable to solve today's economic problems in the EU as well as in the Eurozone, but are having a tremendous impact on the US$-€ exchange rate.

This paper will explain in layman's terms the relationship (or lack thereof) between two of today's most important economic issues: the US dollar and euro exchange rate, and the monetary policy behind it.

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[1] A phrase that John Connally, US Treasury Secretary under President Nixon, used sneeringly to a delegation of European visitors in 1971.

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[2] Helmut Frisch, ¨The Euro and Its Consequences: What Makes a Currency Strong?¨ *Atlantic Economic Journal*, Vol.31, No. 1, (March 03).

[3] The Federal Reserve Bank (Fed) and the European Central Bank (ECB)

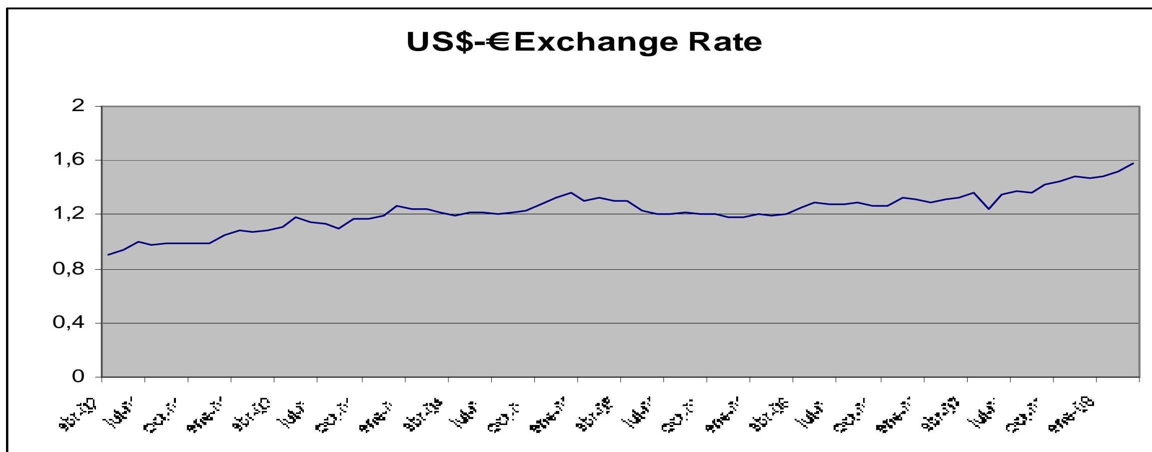
The current state of affairs between the US dollar and the euro

In today's globalized world, countries operate in *open economies;*[4] that is, economies interact freely with other economies. This interaction among countries takes place in two markets. On the one hand, countries buy and sell goods in world *product markets*. This action is measured by the "*trade balance*" account—also known as net exports, or the difference between imports and exports. On the other hand, countries interact among themselves by buying and selling capital assets—such as bonds and stocks—in the *financial markets*. This action is measured by the balance in the *"net capital outflow"* account. The performance of different countries in these two markets is affected by the *exchange rate* of one currency vis-á-vis another currency, which is determined in the *foreign exchange market*.

The foreign exchange market determines the exchange rate between two currencies. Goods, services, and assets produced in a country are not only consumed domestically. Rather, due to the open market economy, they could be consumed abroad; therefore, they must be paid for in the producer country's currency. In order to make these international payment transactions, currencies must be exchanged in the foreign exchange market. This will make goods, services, and assets more or less valuable in terms of one another. In fact, as one currency appreciates, the other currency will depreciate. This is the *zero-sum game* that characterizes the foreign exchange market.

Generally speaking, when the currency of a country appreciates, goods, services, and assets become more expensive and more ´difficult´ to sell abroad; that is, less (price) competitive. At the same time, the goods, services, and assets produced by the other country with the depreciated currency become cheaper and ´easier´ to sell abroad, becoming more (price) competitive. These fluctuations in the price of the exchange rate of goods, services, and assets have an important implication in many areas of the economy of both countries, especially in the trade balance account.

The current exchange rate between the US dollar and the euro is stirring a debate among economist, scholars, and politicians regarding the future of both economic blocs. Nowadays, the exchange rate between the US dollar and the euro is considered unprecedented. The graph below shows that the euro has never reached such a high level against the US dollar since its creation. The debate is how this level is affecting the economies of the US and the Eurozone.



Source: The data was collected manually from e-Signal data provided (www.esignal.com) and was recorded in Excel to create the above graph.

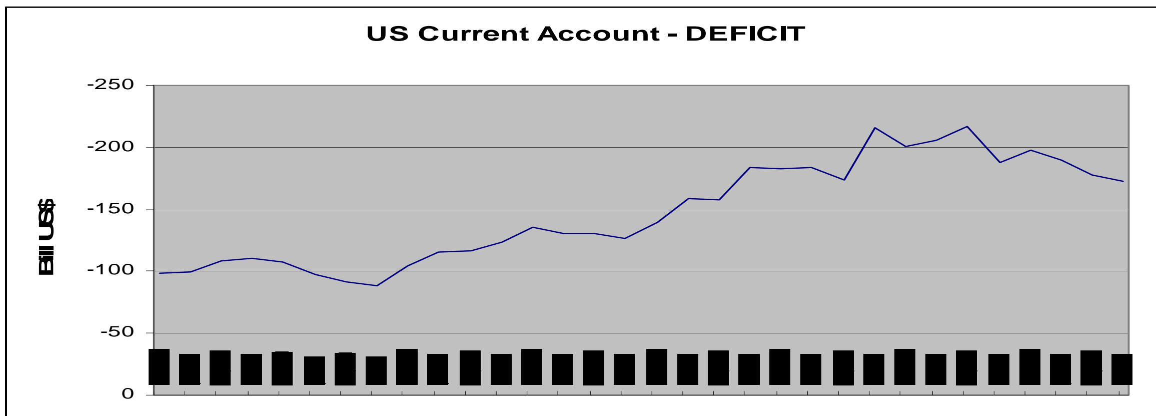
[4] Most of the world's countries are open economies while only a few such as North Korea and Cuba are considered closed or semi-open.

The two sides of the debate and the geopolitical implications

While months ago the appreciation of the euro (when it rose above $1.50) was welcomed on both sides of the Atlantic, now both begin to worry. The analysis of the high euro, or more precisely, the collapse of the dollar, on the product and financial markets of the Eurozone and the US show that this situation is no longer offering a benefit to either country. This lopsided market has become the central topic of discussion for the last months.

The current exchange rate has scholars, economists, and politicians divided. On the US side, Martin Feldstein argues that the decline of the US dollar has come at the right time. In his opinion a weak dollar "is not only a godsend that comes at the beginning of a slowdown, but it will also make it easier to finance the *current account deficit*."[5] He has further asserted that the US needs a competitive dollar; that is, "an exchange rate that will make American goods more attractive to foreign buyers and that will cause American consumers and firms to choose American made goods and services."[6]

Economic theory explains that *current account deficit* is the result of a country´s negative net sale, which means that the country is, in general terms, importing—buying—more that exporting—selling—such as in the case of the US[7]. On the other hand, if the country enjoys positive net sales, it means that the country is exporting more than it is importing, and it will run a trade surplus, i.e. a *current account surplus*, as is the case of the Eurozone.

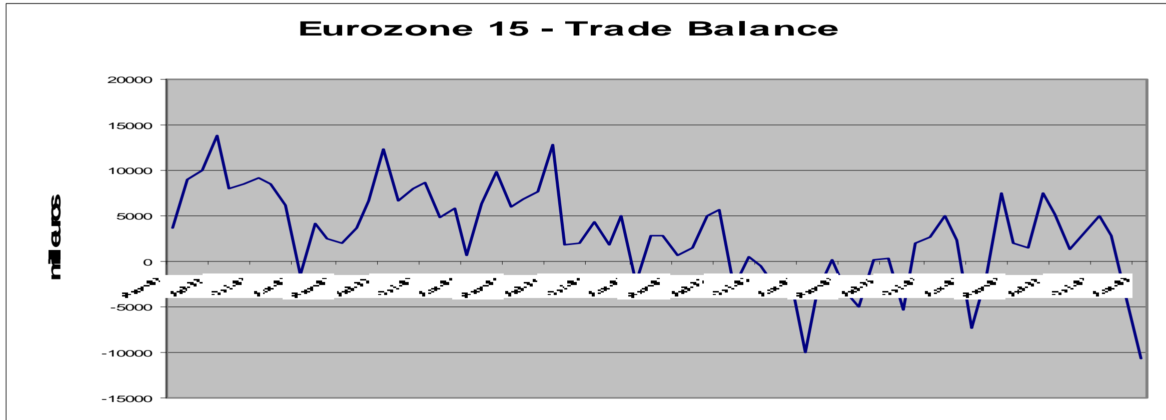


Source: The data was collected manually from The Bureau of Economic Analysis (www.bea.gov) and was recorded in Excel to create the above graph.

[5] Eurointelligence, "Martin Feldstein on the Dollar," March 28, 2008. http://www.eurointelligence.com/article.581+M50b4edc2d93.0.html (Accessed April 2, 2008)

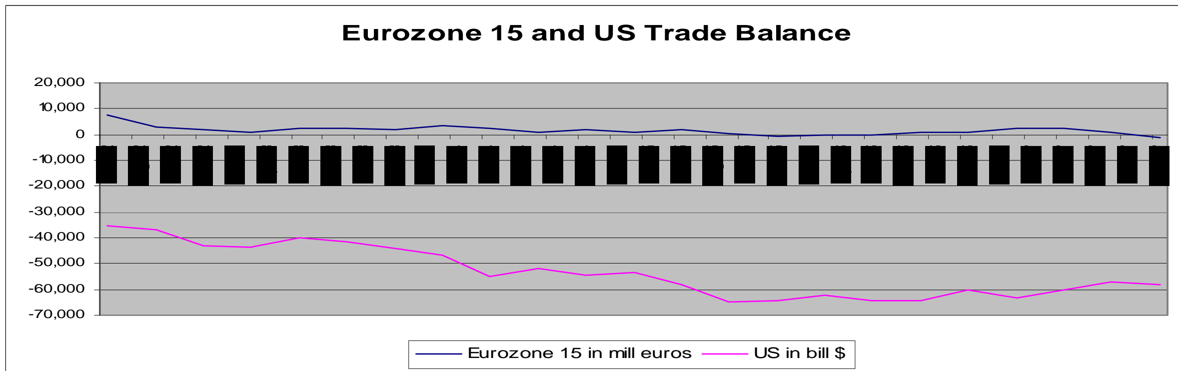
[6] Martin Feldstein, "The Case for a Competitive Dollar," *National Bureau of Economic Research*, http://www.nber.org/feldstein/siepr319.pdf (Accessed March 27, 2008).

[7] The all-time high was reached in 2005 when the US current account was close to US$800 billion, almost 7% of US Gross Domestic Product (http://www.epi.org/content.cfm/webfeat_econindicators_capict_20060616)



Source: The data was collected manually from Bloomberg and was recorded in Excel to create the above graph.

In broad terms, the current account[8] is the result of the sum of the *Trade Balance account* known as net exports (NX) among other accounts. Net exports measures whether a country is a seller or a buyer in world markets of goods. The graph below shows how the Eurozone 15 has been until recently a net seller while the US has been a net buyer.



Source: The data was collected manually from Bloomberg and was recorded in Excel to create the above graph.

The strong dollar is placing the US economy in the middle of an export frenzy that is contributing to the reduction of the deficit from 6.5% of GDP in 2006 to an estimated 4.5% by the end of 2008 - a deficit that has been aggravated by the cost of the Iraq war[9]. However, it has been reported that on March 15, 2008 when the exchange rate between the US dollar and the euro reached $1.56 per euro, the US economy lost "the title of 'world's biggest economy' to the eurozone"[10] In 2007, US authorities reported an official Gross Domestic Product (GDP) estimate of $13,843,800 billion and the Eurozone authorities reported €8,847,889.1 billion. The GDP of the Eurozone at the official exchange rate reported on March 14, 2008 of $1.5688 means that GDP of the Eurozone is $13,880,568.4 billion and surpasses that of the US.

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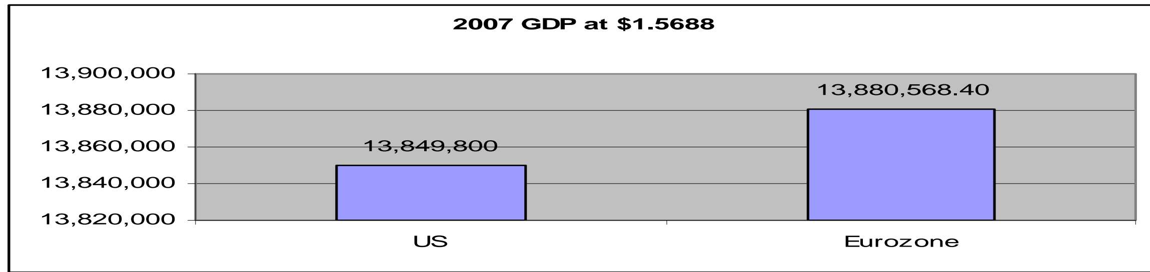
[8] Current Account ={(merchandise trade balance or trade balance) + (balance of payment of services)} + (net international transfer payments) + (net international factor income)

[9] that had it worked out as the WWII, it would have most probably lead to a *"Marshall Plan-like"* agreement between the US and the Middle East

[10] Pax-Europa, "Eurozone Overtakes US Economy," http://pax-europa.com/?p=91 (Accessed April 11, 2008)



Source: The data was collected manually from Bloomberg and was recorded in Excel to create the above graph.

Despite the strong euro, Almunia and Trichet have both made clear announcements that the economic situation of the Eurozone, and consequently of the EU, is a major concern. In fact, Almunia[11] has stated publicly that the good economic times are over[12], and even confirmed that the Eurozone has begun to weaken.[13] In fact, the latest projection of economic growth for the Eurozone has been trimmed continuously from the 2.5% reported in 2007[14] to the 1.8% reported in March, 2008.[15] Trichet has further supported this position and even emphasized that unfortunately the worst is not behind us just yet.[16] Additionally, Trichet reported that "we are concerned about excessive exchange rate moves."[17]

Despite the optimism of the chart above, Sebastian Dullien and Daniela Schwarzer explained in Eurozone Watch[18] that the euro's strength against the US dollar is now seen as a problem. Most European finance and economic ministers believe that this appreciation is posing great threat to the growth prospects of the Eurozone, especially in the current turbulent economic times.

The issue at debate is that such a high euro is having a negative impact for *Eurozone's producers and exporters* of goods and services because it is less competitive. Nevertheless, Germany has experienced an unprecedented export growth and is maintaining a superb industrial production performance. Germany experienced the fastest growth rate in 16 months with 3.8% in January 2008 compared with December 2007.[19] This sends the signal that there is continued demand for German products regardless of the exchange rate. This is, unfortunately, not the case for the rest of the Eurozone countries which, due to the high euro, lack of productivity and competitiveness, are witnessing a deterioration of their trade position. Hence, the performance of Germany, regardless of the high euro, is reminding many of the famous "flight to quality" typical of the US dollar-Deutschmark exchange rate. Jens Ulbrich[20] maintained that the strong euro is irrelevant to the success of German exports because what matters is the global demand for the type of products that Germany specializes in.[21]

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[11] Alain Faujas, "Selon Bruxelles, la zona euro commence a être ébranlée," *Le Monde*, March 28, 2008.
[12] "Le bon temps économiques est terminé"
[13] "La zone euro commence a être ébranlée"
[14] EU Business, "EU Cuts 2008 Eurozone Growth Forecast to 2.2 per cent," November 09, 2007. http://www.eubusiness.com/Finance/1194607021.0/ (Accessed March 27, 2008)
[15] BBC News, "EU Cuts 2008 Eurozone Growth Rate," February 21, 2008. http://news.bbc.co.uk/2/hi/business/7257119.stm (Accessed March 27, 2008)
[16] "Je ne dire pas que le pire est derrière nous."
[17] Reuters, ¨ ECB Is Worried About Excessive Currency Moves,¨ *CNBC,* March 10, 2008. http://www.cnbc.com/id/23558019/ (Accessed March 10, 2008)
[18] Sebastian Dullien and Daniela Schwarzer, "The Euro's Strength: An issue for the EU Summit," March 9, 2008. http://www.euro-area.org/blog/?p=128 (Accessed March 22, 2008)
[19] Ralph Atkins, "Exports Rise Boosts German Economy," *The Financial Times*, March 11, 2008. http://www.ft.com/cms/s/0/46fe8444-ef0b-11dc-97ec-0000779fd2ac.html (Accessed March 11, 2008)
[20] Deputy Head of Economics at the Bundesbank
[21] Ralph Atkins, "Exports Rise Boosts German Economy," *The Financial Times*, March 11, 2008. http://www.ft.com/cms/s/0/46fe8444-ef0b-11dc-97ec-0000779fd2ac.html (Accessed March 11, 2008)

Source: The data was collected manually from Bloomberg and was recorded in Excel to create the above graph.

This strong euro has, on the other hand, had an impact on *consumers and importers* as well. Wyplosz[22] wrote that the strong euro, although it is bad news for the exporters,[23] is excellent news for consumers[24], because the prices of the goods and services imported from the «zone dollar» are now cheaper for the consumers because they are now cheaper to be imported.[25] Therefore, a strong exchange rate strengthens consumer demand, which had been chronically weak in the Euro-area.

The current appreciation of the euro is also playing a *geopolitical role* that is debated by those defending US economic unilateralism vs. those defending multilateralism in the world economy. Munchau opened the debate with one of his columns in the Financial Times. He explained that given the present course of events in the US$-€exchange rate, the dollar might lose its status as *global reserve currency* to the euro. In that case, the "potential geopolitical implications of such a projected shift are immense."[26] However, Benjamin J. Cohen believed that the likely scenario is not one where the euro is replacing the US dollar as global reserve currency. Rather, Cohen proposed a scenario composed of an eroded dollar competing "with several currencies in contention and none clearly in the lead – an increasingly *leaderless* mix of currency relationships." [27] Robert Mundell has recently explained during the "*X Encuentro International de Economistas, Globalizacion y Problemas del Desarrollo"* that took place in La Havana in March 2008, along the line of the precursor of the euro and the common currency area theory, that the current economic situation might eventually lead to the emergence of a new currency he named the INTOR. It will be interesting to see if this new currency proposal is the beginning of what could be called *"Mundell III"*. This is "a new international currency based on a basket integrating the dollar, euro, yen and pound sterling, which would be the basis for a renewed monetary system on the planet."[28]

Eichengreen and Flandreau, on the contrary, claimed that the demise of the US dollar is not close and that the current American's financial crisis and the dollar's depreciation are not bringing

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[22] Charles Wyplosz, "Bonne nouvelle: l'euro est fort!," *Telos*, March 28, 2008. http://www.telos-eu.com/fr/article/bonne_nouvelle_l_euro_est_fort (Accessed April 3, 2008).

[23] "une mauvaise nouvelle pour nos exportateurs qui doivent serer leurs marges"

[24] "c'est un excellente nouvelle pour nous tous, les consommateurs"

[25] "les prix des produits importes de la zone dollar sont devenus moins chers, du moins les importateurs payaient beaucoup moin."

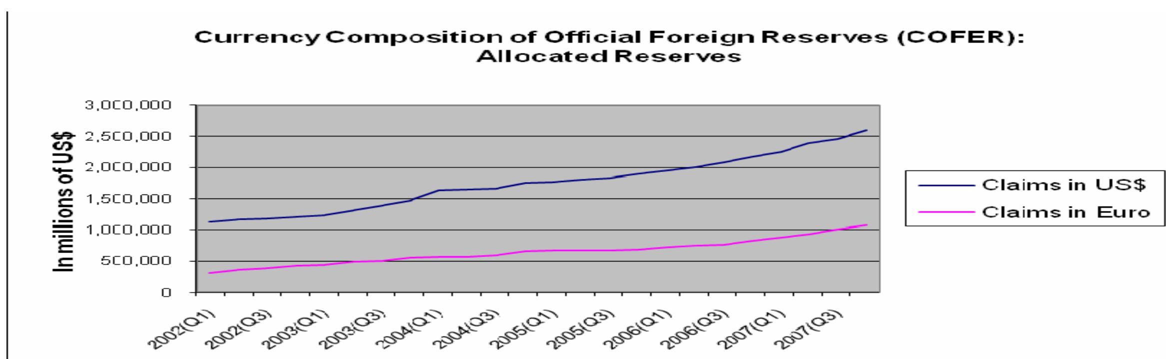
[26] Wolfgang Munchau, "This Crisis Could Bring the Euro Centre-Stage," *The Financial Times*, March 23, 2008. http://us.ft.com/ftgateway/superpage.ft?news_id=fto032320081132135095&page=2 (Accessed April 3, 2008)

[27] Benjamin J. Cohen, "Toward a Leaderless Currency System," March 2008. http://www.polsci.ucsb.edu/faculty/cohen/working/pdfs/Dollar_challengers_rev2.pdf (Access April 1, 2008)

[28] Haydee Leon Moya, "A Space for Diversity of Opinions," *Digital Granma International*, http://www.granma.cu/ingles/2008/marzo/mar18/11economistas-i.html. (Accessed April 2, 2008)

the US to “a tipping point where the greenback will lose its international currency mantle to the euro.”[29] They argue that since the US dollar overthrew the Pound Sterling as reserve currency around 1924-1925, the dollar has only lost this role briefly in the 1930’s “because of disastrous mismanagement of the US economy.” Now, they believe, that despite all the gloom and doom, the economic situation is not that disastrously mismanaged as to cause the euro to overtake the US dollar’s leading role as global currency.

The graph below shows the evolution in the Currency Composition of Official Foreign Exchange Reserves (COFER)[30] reported by the IMF[31].



Source: International Monetary Fund. This graph has been elaborated on by the author. The data used for this graph can be found at http://www.imf.org/external/np/sta/cofer/eng/cofer.pdf, and has been graphed using Microsoft Excel.

Nonetheless, the US dollar’s weakness is stirring an intense debate among OPEC countries as they are wondering with great concern “whether they should maintain their traditional links to the dollar.”[32] More precisely, some OPEC members, particularly Iran and Venezuela, “have proposed trading oil in a basket of currencies to replace the historic link to the dollar.”[33] This is just wishful thinking by those few countries that seek to embarrass and undermine the US. However, the real problem will come if countries such as Saudi Arabia, the United Arab Emirates, or Qatar decide that “they should abandon or revalue their currency pegs to the dollar.”[34]

The forecast is that the US dollar might lose its role as a global reserve currency if the Fed continues with its current monetary policy. However, US authorities do not see any danger in the current monetary policy and dismiss the idea that the euro could replace the US dollar as a global currency, because they view the Eurozone as lacking the strategic power that a global currency demands.[35] Nonetheless, Otmar Issing stated that it is true, while “nobody knows what will happen in ten years from now, … this process of substituting a leading currency with another one is a long process.”[36]

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[29] Barry Eichengreen and Marc Flandreau, “Why the Euro is Unlikely to Eclipse the Dollar,” *The Financial Times*, April 2, 2008. http://www.ft.com/cms/s/0/14049bf2-00b1-11dd-a0c5-000077b07658.html (Accessed April 2, 2008)

[30] COFER is a database that reports “on the currency composition of official foreign exchange reserve.”

[31] International Monetary Fund, “Currency Composition of Official Foreign Exchange Reserves (COFER),” http://www.imf.org/external/np/sta/cofer/eng/index.htm (Accessed April 11, 2008)

[32] David Hale, “Where the Dollar’s Decline Is Taking the World,” *The Financial Times*, November 23, 2007

[33] Sebastian Abbot, “OPEC leaders debating replacement of U.S. dollar,” *The Miami Herald*, November 17, 2007

[34] “What to Do About Opec’s Dollars,” *The Financial Times*, November 20, 2007

[35] The Financial Times, “Looming Dangers for the Dollar,” *Editorial*, March 31, 2008. http://www.ft.com/cms/s/0/1ee9914a-ff4d-11dc-b556-000077b07658.html (Accessed April 1, 2008)

[36] Ralph Atkins, “ Dollar’s Role Is Safe from Euro Challenge,” *The Financial Times*, November 23, 2007

The exchange rate and its relationship with monetary policy

It is generally agreed that a collapsing dollar benefits no one on either side of the Atlantic, and that current monetary policy movements on the US side are not helping the case either. The current monetary policy of the US is trying to prevent the country from a looming recession. How and why? Theoretically speaking, monetary policy is that policy used by a country's monetary authority[37] to manage the supply of money; that is, the amount of money circulating in the economy. The ability to control this supply is paramount because changing the amount of money in circulation helps adjust and prevent economic imbalances such as unemployment, inflation, etc.

Economic theory explains that monetary policy uses a combination of three tools[38] to implement two types of monetary policies: expansionary and contractionary. Each one of these policies is designed to correct a particular economic imbalance. Of those three tools, "*interest rate*"[39] is the most commonly used. Interest rate in layman's term is the *price of money*. When monetary authority reduces interest rates they make 'saving' less attractive. If there is less incentive to save, more money will, in turn, be spent. This will boost investment and consumer spending to increase aggregate (total) demand of goods and services. Consequently, the monetary authority helps fight unemployment and any recessionary shadow. This is called an expansionary monetary policy because it injects money into an economy to stimulate it. On the other hand, the monetary authority can increase interest rates, making "saving" more attractive, in order to constrain investment and consumer spending to decrease aggregate (total) demand of goods and services. This, in turn, will help combat inflation. This is called a contractionary monetary policy because it drains money out of the economy to slow the economic pace.

	Expansionary	**Contractionary**
Interest rates	Reduce	Increase

Currently, the Fed in the US is implementing an aggressive expansionary monetary policy while the ECB in the Eurozone is opting for a neutral—some argue contractionary—one because each economic bloc is suffering from a different kind of economic illness.

While the Fed is trying to keep the US from entering the recessionary phase of the business cycle, the ECB is trying to keep eurozone economies in line with inflation targets set in the Maastricht criteria. Hence each monetary authority is using different tools to achieve different goals and, as a consequence, the exchange rate US$-€is affected.

Trichet explained that there is little prospect of a reversal of the current exchange rate situation any time soon because he sees no motivation at the moment by US monetary authorities to help stop the current decline of the US dollar. Charles Wyplosz denounced the unprecedented lack of cooperation between the Fed and the ECB.[40] He suggested that the Fed´s aggressive monetary policy, which in his opinion is not even working to solve current economic imbalances in the US, is putting the ECB in a very difficult position. Daniel Gros declared that the major differences in monetary policies undertaken by the Fed and the ECB rest on "the mandate of the

[37] The central bank in most developed countries. In the Eurozone is the European Central Bank (ECB), in the US is the Federal Reserve Board (Fed), in the UK is the Bank of England, and in Japan is the Bank of Japan.

[38] Discount rates, open market operations, and reserve requirements.

[39] For the ECB is the "Repo Rate" currently at 4% and for the Fed is the "Fed Funds Rate" currently at 2.25%

[40] Charles Wyplosz, "The Fed Is Delaying the Day of Reckoning," *The Financial Times*, march 12, 2008. http://www.ft.com/cms/s/0/5e9f14d6-f039-11dc-ba7c-0000779fd2ac,s01=1.html (Accessed April 1, 2008)

two central banks."[41] For the Fed is to "provide the nation with a safe, flexible and stable monetary and financial system."[42] For the ECB the mandate is to maintain inflation under control.

This explains why the Fed is cutting rates while the ECB is maintaining them at a high level despite the shadow of economic slowdown. However, on the US side, John Authers noted that never before has the Fed cut interest rates by such an amount when they were already so low.[43] On the Eurozone side, Daniel Cohen recommended that the European Central Bank should cut interest rates now rather than wait for stronger signs of economic slowdown in the future.[44]

In the US, the intention behind the expansionary policy is to stimulate investment and personal consumption especially because experts are crying 'recession'. This recession is caused by the current financial crisis during which the fed has acted as a "lender of last resort" to avoid a second '*Crash of 1929*'. The collapse of the stock exchange indexes means that companies are suffering economic loses which will be translated into millions of jobs lost, with a tremendous negative impact on the unemployment rate and economic growth. This financial crisis is the result of a combination of unfortunate economic events—which manifest the idea behind the 'self-organized critically' theory[45]— such as rising oil prices, slowdown in consumption, and a dramatic drop in real estate markets. These circumstances are, therefore, pressing the Fed to implement expansionary monetary policy with radical interest rates cuts. However, this 'hard medicine' is not having the desired effect just yet on 'the patient' because the credit markets crunch has just started and the financial market is still in disarray. Therefore, by reducing interest rates, the Fed is fundamentally reducing the *price* of money which has a double consequence. First, with lower interest rates, those people paying a mortgage will feel a relief in their monthly mortgage payments. Since they now have a lower payment, they will enjoy an increase in their disposable income. By spending that extra money, they are going to activate consumption. This is particularly beneficial for all those involved in real estate property. Further, lower interest rates are going to motivate investments. People are going to see how their savings are less 'rewarded'. Therefore, since they are not getting a higher price for saving money, they might as well invest it to get a higher reward on the investment. Hence, by reducing interest rates the Fed is injecting money in the economy by making both consumption and investment more attractive than saving. The second consequence of this monetary policy is that interest rate cuts are dragging down the US dollar because cuts are making the US dollar less attractive as an investment instrument. All these 'made in USA' circumstances are impacting the rest of the world as well, and particularly the Eurozone.

From the point of view of the *product market*, the continuous depreciation of the US$ is benefiting the US trade balance. However, from the point of view of the *financial market*, US dollar-denominated investments are being substituted by euro ones. In layman´s terms, investing in the US dollar has a doubly negative impact: a falling dollar accompanied by interest rates paid on the investment of about 2%. This is making investors look for more attractive places to put their money, mainly in the Eurozone. Eurozone financial instruments have become much more 'attractive' because investors are getting interest rates of around 4% and a currency that is, so far, constantly appreciating. Investing in the Eurozone has a doubly positive economic impact, and, in fact, it is a clear trend because ¨se está sacando el dinero de EEUU para invertir en áreas en las que

[41] Daniel Gros, "Different Dilemmas in America and the Eurozone," *The Financial Times*, March 25, 2008. (http://www.ft.com/cms/s/0/e995dd30-fa8a-11dc-aa46-000077b07658.html?nclick_check=1 (Accessed April 4, 2008).

[42] Daniel Gros, "Different Dilemmas in America and the Eurozone," *The Financial Times*, March 25, 2008. (http://www.ft.com/cms/s/0/e995dd30-fa8a-11dc-aa46-000077b07658.html?nclick_check=1 (Accessed April 4, 2008).

[43] John Authers, "The Short View: Wall St and Fed," March 18, 2008. http://www.ft.com/cms/s/0/0393ce94-f532-11dc-a21b-000077b07658.html (Accessed March, 22, 2008)

[44] Eurointelligence, "Dragui's List," March 2, 2008. http://www.eurointelligence.com/article.581+M56925be519b.0.html (Accessed April 3, 2008)

[45] This theory explains that "economies posses intrinsically unstable dynamics, which even in the absence of external shocks would result in persistent deterministic fluctuations" in Jose A. Scheinkman and Michael Woodford, "Self-Organized Critically and Economic Fluctuations," The American Economic Review, Vol. 84, No. 2, May, 1994, pp. 417-421

el precio del dinero está evolucionando al alza, con el objetivo de obtener mayores rentabilidades.¨[46]

Final Word

The US and the Eurozone are suffering from different economic illnesses with a common denominator. Both economic blocs are experiencing an economic slowdown that is pushing the US and the Eurozone to the verge of an economic recession.

For the US, this recession is caused by economic slowdown aggravated by a financial crisis due to the collapse of stock exchange indexes, particularly the Dow Jones ($Indu), which reminded many of a second '*Crash of 1929.*' The Eurozone is trying to pull the Eurozone out of a very difficult situation caused not only by the high euro but also by the lack of productivity and competitiveness - problems that the Eurozone should correct. Otherwise, low productivity and competitiveness together with laxity in the observance of the requirements of the Stability and Growth Pact will put the Eurozone in a very difficult economic situation that will ultimately destroy the trust that the euro has been gaining lately. As Milton Friedman explained, the ultimate goal of every government is to obtain and maintain unquestionable trust and value on its national currency.[47]

Further, the US, the Fed and the US dollar cannot cope alone with the demands of globalization as the *lender of last resort*. Modern economic problems are mainly caused because the US$ has become *everybody´s problem*, and hence require innovative economic solutions. One solution could be *economic multilateralism* between major world economic authorities such as US, Eurozone, Britain, Japan and even China. This is not multilateralism from a *new-left-populist* perspective, but rooted on the ideas expressed by Mundell last March 2008 in La Havana which seems to be a possible nascent '*Mundell III*'. This multilateralism might be the *deus ex machina* necessary to solve today´s global economic imbalances.

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[46] M. Martínez, ¨China dispara al euro al borde de 1,50 dólares,¨ *Expansión,* 8 Noviembre 2007.

[47] Milton Friedman, "The Island of Money," in Money Mischief: Episodes in Monetary History, New York: Harcourt Brace Jovanovich, 1992.