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Greenspan Says Weaker Dollar May Help Narrow Trade Gap

By REUTERS

WASHINGTON (AP) -- Federal Reserve Chairman Alan Greenspan said Tuesday that a weaker U.S. dollar should eventually help narrow the country's swollen trade deficit and renewed a warning that "creeping protectionism" could hurt the flexibility of the global economy.

In remarks to the Economics Club of New York, Greenspan said the value of the U.S. dollar, compared with the currencies of this country's major trading partners, has declined about 12 percent from its peak in early 2002. A weaker dollar makes U.S. goods cheaper to foreign buyers and makes foreign-made goods more expensive to U.S. buyers.

"The currency depreciation that we have experienced of late should eventually help to contain our current account deficit as foreign producers export less to the United States," Greenspan said. "On the other side of the ledger, the current account should improve as U.S. firms find the export market more receptive."

The country's current account deficit -- the broadest measure of trade-- hit $550 billion last year, requiring the United States to borrow that amount from foreigners during a period when the dollar was weakening in value.

Many private economists are concerned that if foreigners suddenly become spooked and start dumping their U.S. holdings, stock prices could plunge and interest rates soar.

Greenspan, however, said that as long as a flexible international financial system is maintained -- something that has allowed the United States and other countries to weather economic hard times -- problems should be avoided.

"History suggests that the odds are favorable that current imbalances will be defused with little disruption to the economy or financial markets," he said.

A copy of his remarks was distributed in Washington.

Greenspan did not address the future course of interest rate policy in the United States or the current state of the economy.

His remarks come at a time of rising tensions surrounding globalization and the world's trading climate. "It is imperative that creeping protectionism be thwarted and reversed," he said.

On China, Greenspan cautioned that if the country were to swiftly move to let its currency float freely, it could pose a further risk to the country's fragile banking system and to the global economy.

The Bush administration has been pressing Beijing to stop linking its currency, the yuan, to the dollar and instead let the value of the yuan be set in open markets.

"Many in China, however, fear that an immediate ending of controls could induce capital outflows large enough to destabilize the nation's improving, but still fragile, banking system," Greenspan said. "Others believe that decontrol, but at a gradual pace, could conceivably avoid such an outcome."

China's banking system is currently in weak condition, and abruptly removing the currency peg now in place could make that worse, Greenspan had said in a letter to Senate Banking Committee Chairman Richard Shelby, R-Ala.

As much as 50 percent of Chinese bank loans are estimated to be nonperforming, Greenspan said.

The United States' politically sensitive deficit with China in 2003 was almost $124 billion, the biggest ever, as imports from China hit a record high. By country, the U.S. trade gap with China was the largest.

America's manufacturers contend that China is deliberately undervaluing its currency by as much as 40 percent. That would give China a big trade advantage when competing with U.S. companies and would contribute to the loss of U.S.

factory jobs.