he dollar goes up, the dollar goes down. Recently, it’s down. From Jan. 2, 2002, through March 7, 2003, the dollar fell by 20 percent against the euro, 10 percent against the pound sterling and 13 percent against the Japanese yen. Historically, such fluctuations are not unusual, though they are seldom easy to explain.

Ask an economist to describe the reasons for the greenback’s recent decline, and the reply will include a furrowed brow. Few subjects are as complicated or confounding to us as the foreign currency exchange rate market—the deepest, most liquid and one of the least regulated markets in the world.

Each day, more than $1 trillion in currency trades in the foreign exchange market. Many participants and factors affect the value of one currency versus another. The market consists of a worldwide cast of businesses, investors, speculators, governments and central banks acting and reacting based on a mix of forces such as trade patterns, interest rate differentials, capital flows and international relations.

As the dollar has recently undergone its worst slide against European currencies since 1987, the overarching reason can be attributed to a reduced demand to place investment funds in the United States, a situation quite different from that of the late 1990s. Between 1995 and 2000, the attractiveness of U.S. capital markets resulted in the dollar rising 20 percent against other major currencies. But recently, with the decline in the U.S. stock market, as well as lower interest rates on U.S. government securities, outside investors have turned skittish. Other confidence crushers include last year’s corporate accounting scandals and rising tensions with Iraq and North Korea.

A weakened dollar, despite the negative connotation, does carry certain benefits. Although American travelers and businesses are not able to stretch their money as far on foreign soil, the opposite is also true: Foreign consumers are able to purchase more U.S. goods with their own beefed-up currency. Such behavior, in theory, should help reduce the U.S. trade deficit, which swelled to a record $44.2 billion in December 2002.

So which is preferable, a strong dollar or a weak dollar? To answer this question, let’s distinguish “strong” from “rising” and “weak” from “falling.” It makes no sense to interpret “strong dollar” to mean an exchange rate that is rising at a rapid pace forever. That would take the currency far away from any reasonable equilibrium.

What we must mean by a strong dollar is an exchange rate that is on average relatively high, and perhaps trending gently upward. That is, in fact, the pattern most often associated with an economy that is performing well. An economy that is growing vigorously, generating many new jobs and creating enticing new opportunities is a good place to invest. That good place tends to attract investment from abroad, and one consequence is a strong currency.

If the dollar’s recent decline can be attributed to the slowdown in the U.S. economy, along with corporate governance and geopolitical uncertainties, which I suspect it can, then recent weakness in the dollar is not a matter for serious concern. As the economy rebounds, I would expect foreign investment to make a comeback, and the dollar with it.

So, remember: The dollar goes up, the dollar goes down. These are normal fluctuations in a well-functioning and vigorously competitive market.

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