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Trade Deficit Stubbornly Defies the Dollar's Slide



Ed Alcock for The New York Times

Breakfast at the popular Café de Flore in Paris cost some recent visitors 46 euros, or about \$60.

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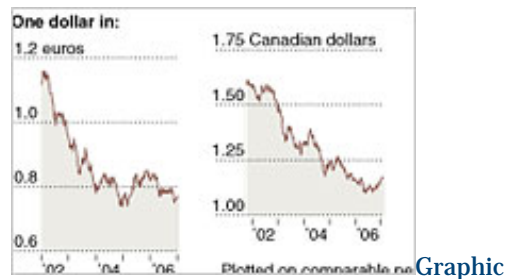
By [EDUARDO PORTER](#) and [MARK LANDLER](#)

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Jessica Heyman's breakfast in Paris last month was nothing out of the ordinary: a modest repast of eggs, coffee and a side salad with her husband, Jonathan Podwil, at the popular Café de Flore. But the bill was memorable — 46 euros, or about \$60, at the current exchange rate. Five years ago, when the dollar was strong, the same bill would have amounted to \$42.

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The sticker shock provided a powerful incentive to remain frugal the rest of the vacation. “We ate a lot of bread,” Ms. Heyman said.

Shocking tourists into counting every penny, and getting Americans back home to spend less on costly imports, is part of what a weaker dollar is supposed to do to help pare America's outsize trade deficit, according to economic textbooks.

But, so far, the dollar's slide has not helped enough. Although the dollar has lost a lot of ground against many of the world's major currencies — including the euro, the British pound and the Canadian dollar — the nation's trade imbalance with the world has continued to rise, reaching \$702 billion in the first 11 months of 2006, on track to easily outstrip the \$717 billion of 2005 and set another record.

Officially, the United States government does not welcome the dollar's weakness. “A strong dollar is clearly in our interest,” the Treasury secretary, [Henry M. Paulson Jr.](#), said last month.

But many economists say that the Bush administration is satisfied with the dollar's fall against the euro and some other currencies, counting on the decline to help improve the competitiveness of American manufacturers in global markets.

For several reasons, however, that may not happen anytime soon — even if the dollar continues to weaken against European currencies. For one thing, the dollar has not fallen much against the currencies of some crucial trading partners, including China and Japan. Critically, the value of China's yuan against the dollar has been carefully managed by Beijing so that it does not increase much more than 5 percent annually against the dollar. That is a reason China alone ran up a \$214 billion surplus in its trade of goods with the

United States from January to November last year.

Many foreign suppliers, moreover, are willing to absorb the impact of a declining dollar on their profit margins rather than pass it on to consumers as higher prices. That gives Americans less of an incentive to shift away from imports.

In the end, for the United States to begin to balance its trade, American consumers must spend less, while foreign consumers would have to buy a lot more.

“My U.S. colleagues tend to believe that exchange rates can carry out this adjustment painlessly which I, looking from the outside, find hard to believe,” said Thomas Mayer, chief European economist at [Deutsche Bank](#) in London. “You would need to have unrealistically large changes in exchange rates to overcome that gap.”

Free market economists argue that the deficit does not really matter — it is mostly a benign side effect of America’s faster economic growth and its appeal as a destination for foreign investment. Trade imbalances are nothing to worry about, these economists say, reflecting private transactions that just happen to occur across borders.

Still, with the deficit now in excess of 5 percent of the nation’s gross domestic product, many other economists worry that the foreign debt needed to finance the growing imbalance is accumulating at an unsustainable pace.

To some extent, a weaker dollar has bolstered American exports to strong-currency nations. America’s inflation-adjusted deficit in trading goods and services with the [European Union](#) declined by about 1 percent in the first three quarters of last year compared with the 2005 period, to about \$84 billion.

And American producers are seeing some benefits. California wineries, for example, have shown double-digit sales growth in Canada every year since 2002, when the dollar started its fall against the Canadian dollar.

“There’s a real price threshold of 10 Canadian dollars a bottle,” said Joseph Rollo, director of the international department at the Wine Institute, the lobby group for California wineries. “A few years ago it was very difficult for California wineries to make that level. Now it’s a lot easier.”

The cheap dollar is also allowing some American companies to enter foreign markets for the first time. Phoenix Closures, a manufacturer of bottle caps in Naperville, Ill., exports very few of its caps to Europe. But a few months ago, it unexpectedly picked up a German client. “I assume these guys are getting a fairly large price reduction coming to us,” said Bert Miller, president of the company.

The opposite side of Ms. Heyman’s expensive breakfast in Paris is that America is now a bargain destination for Europeans.

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Keith Bradsher contributed reporting from Hong Kong, and Martin Fackler from Tokyo.





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