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What the Dollar Strength Could Mean for Gold

- Carol Roth

In this informative newsletter, Carol covers why the US dollar isn't as strong as you might think; how the dollar's status is likely to change; how Fed and government policy will impact the dollar going forward; how US's recent actions and reserve currency status should be impacting your thinking; and more!

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The dollar is currently the "cleanest shirt in the laundry"

Michael Burry, the famed investor from "The Big Short" who was an early predictor of the 2008-2009 Great Recession, said a couple of months ago in a tweet, "When you see mention of the strong dollar, the almighty dollar, please remember this is only in relation to other fiat currencies. The dollar is not at all strong, and it is not getting stronger. We all see it every single day in prices of everything."

This is what some call being the "cleanest shirt in the laundry".

The global macroeconomic backdrop, with a combination of much of the world's food, oil and other commodities, as well as debt, being denominated in dollars and the faltering of other currencies (based on careless global central bank actions and fears of a global recession), puts the dollar in an extraordinary, although likely temporarily unique, position.

As the Federal Reserve has begun to raise the Fed Funds interest rate and signaled their willingness to do more, along with the volatility being seen in markets worldwide, more investors have, for the time being, sought some perceived safety in the dollar.

However, over the long-term, the dollar contends with a number of issues that threaten its standing as a safe haven and make a good case that you should consider adding gold and other diversified assets to your portfolios.

The dollar's purchasing power destruction

While it is the cleanest shirt in the laundry in terms of other currencies, in terms of your buying power, the value of the dollar is continually being destroyed. The policies of the government and the Federal Reserve, including running up and monetizing our debt, have made your dollar worth less and less in terms of the goods and services that it can purchase.

You don't need economists to tell you this-you can see it in your everyday cost of living. Your dollar doesn't go nearly as far as it did a decade ago. A decade ago, it didn't go nearly as far as two decades ago, and so on.

But even though people can see this happening, they sometimes forget the implications and to judge purchasing power vis-à-vis investments. Billionaire investor and founder of the hedge fund Bridgewater Associates, Ray Dalio, said in an interview with Insider, “Investors make the mistake of judging their wealth in the number of dollars or pounds or whatever currency they're looking at it. They should judge it in relationship to buying power. They make serious mistakes if not, particularly in judging the riskiness of cash."

You may be told the dollar is strong, but your purchasing power knows otherwise.

The spending keeps on coming

It’s not as though the government has learned any lessons about overspending, either. Federal government spending for Fiscal Years 2020 and 2021 were “distorted” with covid relief funds, yet for Fiscal Year 2022, the budget, according to the White House’s website, Historical Tables 1.1, is projecting that the federal government will spend $5.8 trillion for the year!

$5.8 trillion in spending is 25% of last year's GDP (a fair proxy, as we know GDP is down in the first two quarters of calendar 2022). It is also a projected deficit of $1.4 trillion, which we know will ultimately be financed with more debt. That deficit is a 44% increase over the already insane pre-covid 2019 deficit of $983 billion.

And, with new spending proposals being trotted out by Congress, fiscal responsibility is nowhere near their vocabulary or principles.

The Fed’s old habits will likely die hard

On top of the rampant government spending, and despite tightening monetary policy conditions, most economists don’t think that will last. Economists surveyed by business media outlets are finding that the majority of them believe that the Federal Reserve will reverse course start to cut their Fed Funds rate by the end of 2023!

Should that happen, investors who have been running to the supposed “safe haven” of the dollar will also likely shift course when they sense this change is on the horizon.

With the Fed indirectly impacting the cost of government debt and the interest cost to service that debt, they have a quiet but obvious reason to keep rates lower long-term.

Dollar reserve currency status isn't guaranteed forever

In addition to the above, the US government has treated the dollar as a financial weapon, not managing the dollar in a stable manner as a global reserve currency and threatening the stability of and access to reserves for other countries.

Some countries have intentionally begun to move away from dollar-based reserves and are looking to other options (including other currencies and gold). As time goes on, that puts the US's status as holder of the sole global reserve currency at risk.

As the dollar reverses course, which is likely given the erosion of its purchasing power, again investors will likely turn to other safe havens, which could include gold.

It is critical that investors think long-term about their portfolio strategy and understand the implications related to policy and the dollar, and how it will impact them long-term. The cleanest shirt in the laundry is still dirty. Just because the dollar is showing strength today vis-à-vis other currencies doesn't mean that it isn't without many issues and that its status isn't going to change in the medium-to-long term.

Investing in gold is a long term hedge and diversification tactic, and is part of a balanced portfolio and broader legacy planning strategy. Short term fluctuations in price are to be expected, but it is important to have a broader term view.

If you haven't added or updated your hedges, like gold, recently, talk to a financial advisor or specialist to review your portfolio and make sure that it is well positioned given your risk profile and objectives for the likely volatile times ahead. Also, consider calling my friends at Goldline for more information.