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Currency Manipulation Can't be Fixed By Countervailing Duties

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The Senate is in the process of debating whether to grant the president trade promotion authority (TPA), which would allow Congress to consider trade agreements under “fast track” procedures. Some senators would like to address currency manipulation – artificially reducing the value of a country’s currency to gain an export advantage – during the TPA debate. They propose adding an amendment that would designate currency undervaluation as a subsidy for purposes of calculating margins in countervailing duty (CVD) cases. This would authorize the Department of Commerce to impose CVD duties even when no other subsidies are alleged, thus further restricting imports. Such an approach would be harmful to the economic interests of the United States and appears destined to violate World Trade Organization (WTO) rules. The amendment should be rejected.

The effects of currency manipulation can be counterintuitive. A shift in exchange rates changes a country’s “terms of trade,” which is an expression used by economists to describe the ratio of a country’s export prices to its import prices. From a U.S. perspective, if another country sets its currency at an artificially low level relative to the dollar, the U.S. terms of trade will improve. The United States will be able to obtain a greater quantity of imports for the same quantity of exports. Exporting the same number of airplanes and soybeans as before will pay for the importation of larger quantities of shoes, coffee and flat-screen TVs.

The country that chooses to undervalue its currency will be placing an unrealistically low value on the output created by workers and capital in its domestic economy. It will, in effect, be selling its exports for less than their true economic worth. A nation that is consciously devaluing is making a decision to transfer wealth to the United States. Our country should think twice before rejecting such a gift.

An increase in affordable imports generally doesn't strike consumers as a bad thing. People tend to enjoy the higher standards of living that result from trade. Assuming imports don't compete too directly with goods and services produced widely in the United States (think of bananas, clothing, rare earth metals, etc.), they tend to be well accepted, even by people with mercantilist tendencies. Some imports that do compete directly with U.S. products – such as crude oil or cars – also may not raise strong political objections, either because domestic demand is larger than can be served solely by domestic supplies, or because consumers desire a variety of choices.

The politics become more complicated when imports compete directly with goods and services produced by U.S. firms that are finding it difficult to thrive in the global economy. Firms often struggle to deal with forces as diverse as new technologies or changing consumer tastes and preferences. Companies competing with imports they believe to be unfair often file antidumping or countervailing duty cases. The large majority of such cases result in the imposition of import duties.

Trade remedy statutes already have a pronounced bias in favor of domestic industries. There is no justification for making the law even more protectionist, as would be the case if CVD margins were imposed to offset alleged currency manipulation. Higher duties would hurt firms that rely on imported goods to be used in the manufacture of value-added products. The economics of the situation are clear – businesses and consumers that depend on imports would be harmed more by duties than import-competing businesses would be helped. Imposing higher import duties would result in a net loss for the U.S. economy.

In addition, WTO rules require a subsidy to be "specific" in order for it to be countervailable. This means, for example, that a subsidy must be provided to a specific industry, or for a specific trade-distorting purpose, such as the subsidization of exports. Since the value of a country's currency affects the nation's economy broadly, it seems doubtful that currency manipulation would be specific enough to survive the WTO dispute settlement process. In other words, changing the law to allow the CVD process to be used against currency manipulation would mean that the United States could expect eventually to lose at the WTO.

Despite substantial fluctuations over time in the value of the dollar against other currencies, the United States has prospered and grown as the global economy has become more interconnected. This growth will continue as long as the American economy is free to innovate and is open to world-class competition. Adding import duties to products from other countries would slow rather than advance U.S. economic development.

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