CURRENCY MANIPULATION IN 2016

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1. Currency manipulation was by far the most distorting and unfair trade practice in the world during the decade or so to about 2013. It transferred hundreds of billions of dollars of trade and production, and millions of jobs, to China and other manipulating countries from the United States and other deficit countries.

2. Manipulation declined substantially in 2014, however, and almost disappeared in 2015. China and many other former manipulators were in fact intervening to keep their currencies from falling further rather than from rising. They were frequently selling rather than buying dollars.

3. Market forces explain most of this dramatic change in behavior. The exchange rate of the dollar rose substantially against virtually all currencies in 2014-15 due to the superior performance of the US economy, the termination (and recent initial reversal) of monetary easing by the Federal Reserve, loosening of monetary policy in many other countries (especially the Eurozone and Japan) and growing uncertainty over China and other emerging markets. Hence the currencies of most of our trading partners declined on their own, without any manipulation, in some cases even too far and too fast for their comfort.

4. I suspect that US pressure, especially from the Congress, was also a factor in the sharp decline in manipulation. The United States reacted strongly, for example, to Japan's talking down the yen in late 2012 and China's mini-devaluation of last summer. The Congress of course kept up a steady drumbeat against manipulation throughout the trade policy debate of the past year.

5. We cannot know whether this welcome drop in manipulation will continue when market forces reverse and push the dollar down again, as they surely will over the medium term. It is thus critically important to erect and implement effective deterrents against the practice that will protect our economy from a repetition of the heavy costs levied by manipulation over the past decade.

6. The Congressional debate of the past year has produced (or will presumably shortly produce) two potentially significant changes in US currency policy that should contribute to such deterrence. One, in response to the negotiating objectives included in the Trade Promotion Authority legislation, is the currency side agreement to the TransPacific Partnership announced in November by the Treasury Department. It commits the TPP countries – assuming that the TPP itself is approved by Congress and other parliaments and enters into force as negotiated – to avoid manipulation and to publish the relevant data so their currency practices can be monitored. The new consultative group created by that agreement will meet at least annually and release public reports on its deliberations.

7. The second, potentially even more important, change is the Bennet-Hatch-Carper Amendment to the customs bill – assuming that bill passes the Congress as it recently emerged from the conference committee. That Amendment forces the Treasury to substantially strengthen its response to manipulation by specifying clear criteria requiring the initiation of "enhanced engagement" with manipulators and then requiring the Administration to take action against inadequate response on their part.

8. The Administration, however, retains a great deal of flexibility in implementing both new policies. It is thus imperative that the Congress monitor its performance systematically and insist that it carry out its new mandates aggressively.

9. I would have preferred that more extensive currency obligations would have resulted from the trade debate of the past year. It would be desirable to include enforceable currency disciplines in trade agreements but they apparently could not be negotiated in the TPP. The Schumer Amendment to the customs bill, authorizing countervailing duties against imports subsidized by currency manipulation, would have added to the deterrent effect of US policy. So would "remedial currency intervention" as voted by the Senate in its currency bill in 2011.

10. However, I believe that significant progress can be made against the risk of new manipulation through the steps that are now being adopted. I therefore recommend that the Congress now take three steps:

    a. Pass the TPP as soon as possible, including to activate the side agreement on currency.

    b. Pass the customs bill with the Bennet-Hatch-Carper Amendment as soon as possible to enact the new policy requirements for Treasury.

    c. Set up procedures, including both private consultations with Treasury and public hearings, to systematically monitor and assess the effectiveness of the new policies and the possible need of additional steps as future trade issues, such as the legislation for a Transatlantic Trade and Investment Partnership, come before Congress.