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Debates over Currency Manipulation

Overview

Some Members of Congress and policy experts argue that U.S. companies and jobs have been adversely affected by the exchange rate policies adopted by other countries. They allege that these countries use policies to “manipulate” the value of their currency in order to gain an unfair trade advantage against other countries, including the United States.

Other analysts are more skeptical about currency manipulation being a significant problem. They raise questions about whether government policies have long-term effects on exchange rates, whether it is possible to differentiate between “manipulation” and legitimate central bank activities, and the net effect of currency manipulation on the U.S. economy.

Background

What is currency manipulation? At the heart of current debates is whether or not other countries are using policies to intentionally weaken the value of their currency, or sustain a weak currency, to gain a trade advantage. A weak currency makes exports less expensive to foreigners, which can spur exports and job creation in the export sector.

Can governments weaken their currencies? Economists disagree about whether government policies have long-term effects on exchange rates, particularly for countries with floating exchange rates. However, some economists believe that, at least in the short run, some government policies can impact the value of currencies. One policy is buying and selling domestic and foreign currencies (“intervening”) in foreign exchange markets. A number of economic policies, including monetary, fiscal, and structural policies, may also affect exchange rate levels but they may be pursued for policy goals unrelated to trade. For example, a central bank may adopt expansionary monetary policies to combat a domestic recession, while having the simultaneous effect of depreciating the currency.

What is the impact on the United States? If another country weakens its currency relative to the dollar, U.S. exports to the country may be more expensive and U.S. imports from the country may be less expensive. As a result, U.S. exports to the country may be negatively affected, and U.S. producers of import-sensitive goods may find it hard to compete with imports from the country. On the other hand, U.S. consumers who buy imports and U.S. businesses that rely on inputs from overseas may benefit, because goods from the country may be less expensive.

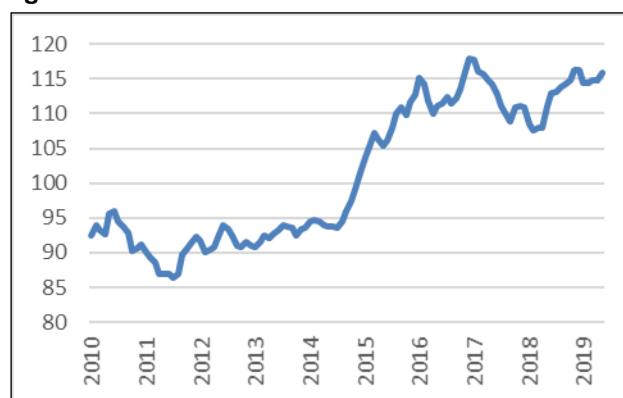
Which countries are accused of currency manipulation?

There is debate over which countries, if any, are manipulating their exchange rates. Part of the debate is which, if any, government policies should count as currency

manipulation. Economists have also developed a number of models to estimate whether the actual value of a currency differs from what it “should” be according to economic fundamentals. Various models produce different results.

According to a 2017 study by economists at the Peterson Institute for International Economics, currency manipulation has largely been in remission since 2014. The Treasury Department since President Trump took office has not formally found any country to be manipulating its currency in its semiannual report to Congress. China's interventions in foreign exchange markets to limit appreciation of its currency largely occurred between 2003 and 2014. However, recent depreciation of China's currency, as well as a relatively strong U.S. dollar (**Figure 1**), may be fueling Administration concerns. A strong dollar makes it more difficult for some U.S. firms to compete against foreign producers.

Figure 1. Nominal Broad Dollar Index



Source: Federal Reserve.

Notes: An increase on the graph represents an appreciation of the U.S. dollar against other currencies.

Existing Policy Frameworks

Multilaterally, members of the International Monetary Fund (IMF) have committed to refraining from manipulating their exchange rates to gain an unfair trade advantage. Violators could face loss of IMF funding, suspension of voting rights or, ultimately, expulsion from the IMF. The IMF has never publicly labeled a country as a currency manipulator. Some argue that commitments made in the context of the World Trade Organization (WTO) are relevant to disagreements over exchange rates, although this view is debated. Exchange rates are also discussed by the G-7 and the G-20, where commitments to refrain from currency manipulation are now routinely emphasized.

Provisions in U.S. law also address currency manipulation. The **1988 Trade Act** (P.L. 100-418) requires the Treasury Department to analyze semiannually the exchange rate policies of major U.S. trading partners. If some countries

are found to be manipulating their currencies, the Act requires the Treasury Secretary, in some instances, to initiate negotiations to eliminate the “unfair” trade advantage. The Act also has a semiannual reporting requirement on exchange rates in major trading partners. Treasury has not found currency manipulation under the terms of the Act since 1994.

The **Trade Facilitation and Trade Enforcement Act of 2015** (P.L. 114-125) adds new reporting requirements and directs the Treasury Department in some instances to take action against countries that have: (1) a significant bilateral trade surplus with the United States; (2) a material current account surplus; and (3) engaged in persistent, one-sided interventions in foreign exchange markets. Some economists contend that, together, these three indicators suggest currency manipulation. To date, Treasury has not found a country that meets all three criteria. However, it has developed a “Monitoring List,” which includes countries that meet two of the three criteria currently or in the past year. The Monitoring List for May 2019 includes China, Japan, Germany, Italy, Ireland, Singapore, Malaysia, South Korea, and Vietnam.

In 2015, Congress included currency as a principal negotiating objective in **Trade Promotion Authority** legislation for the first time (P.L. 114-26). TPA is the authority Congress grants to the President to enter into certain reciprocal trade agreements and to have their implementing bills considered under expedited legislative procedures when certain conditions have been met. Previously, exchange rates were not generally part of trade negotiations.

“We recognize that excessive volatility or disorderly movements in exchange rates can have adverse implications for economic and financial stability. We will refrain from competitive devaluations, and will not target our exchange rates for competitive purposes.”
G-20 Finance Ministers and Central Bank Governors Communiqué, March 19-20, 2018.

Trump Administration Policy Proposals

During the 2016 presidential campaign, Donald Trump raised currency manipulation, particularly by China, as a key issue. Since assuming office, President Trump has continued to express concerns about the exchange rate policies of other countries. The Trump Administration focused its efforts to address unfair currency practices through trade negotiations. Most notably, the proposed United States-Mexico-Canada Agreement (USMCA) includes, for the first time in a trade agreement, provisions on exchange rates, widely viewed as a template for future trade negotiations.

The Trump Administration has proposed new actions to counter what it regards as currency manipulation, with some calling currency conflicts the “next front in the trade war.” In May 2019, the Commerce Department also issued a notice of proposed rulemaking to provide regulatory authority to potentially impose countervailing duties on imports from countries determined by the U.S. government to be acting to undervalue their currency relative to the U.S.

dollar. Public comments on the proposal are being accepted through June 27.

The new tool proposed by the Commerce Department has been discussed for years in Congress. Under current U.S. law, countervailing duties can be applied to imports that have been subsidized by a foreign government. Some argue that currency manipulation is the functional equivalent of a subsidy, and this should also be an “actionable” subsidy under U.S. law (meaning that it is eligible for countervailing duties).

However, applying countervailing duties to imports from countries that manipulate their currencies is controversial. Of the six public comments submitted to date, most, including from a former Treasury official, oppose the proposal. Concerns focus on how it could be operationalized, whether it is consistent with U.S. obligations under the World Trade Organization (WTO), and whether it would help the U.S. economy.

Possible Policy Issues

How should currency manipulation be defined and measured? Analysts debate how to define currency manipulation. Some argue that the IMF’s definition requires it to determine that policies shaping the exchange rate level have been for the express purpose of increasing net exports, and that “intent” is hard to establish. Analysts also disagree on how to calculate or estimate whether currencies are misaligned from their “equilibrium” long-term value, complicating the classification of currencies as over- or under-valued.

Would measures to combat currency manipulation serve U.S. economic interests? Some analysts argue that currency manipulation gives other countries an unfair competitive trade advantage over the United States. Others disagree, arguing that the effects on the U.S. economy are not unambiguously negative. U.S. consumers and U.S. businesses that rely on inputs from overseas may benefit when other countries have weak currencies. They also caution that labeling other countries as currency manipulators could trigger retaliation.

If currency manipulation should be addressed, what is the proper tool or tools? In addition to including provisions in trade agreements and applying countervailing duties, some analysts have called for “countervailing interventions” in foreign exchange markets and/or addressing currency issues more prominently at the IMF or WTO. What are the tradeoffs of the different policy options? Which most effectively address U.S. concerns?

For more information, see CRS Report R43242, *Debates over Exchange Rates: Overview and Issues for Congress*, by Rebecca M. Nelson.

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