Trade and Currency

Can WTO Rules Have a Role?

11.2.2014

Common themes of GATT/WTO

Bali

Tariff

Subsidies

Protectionist measures

Market access

Goods and Services

Technical Barriers

NAMA

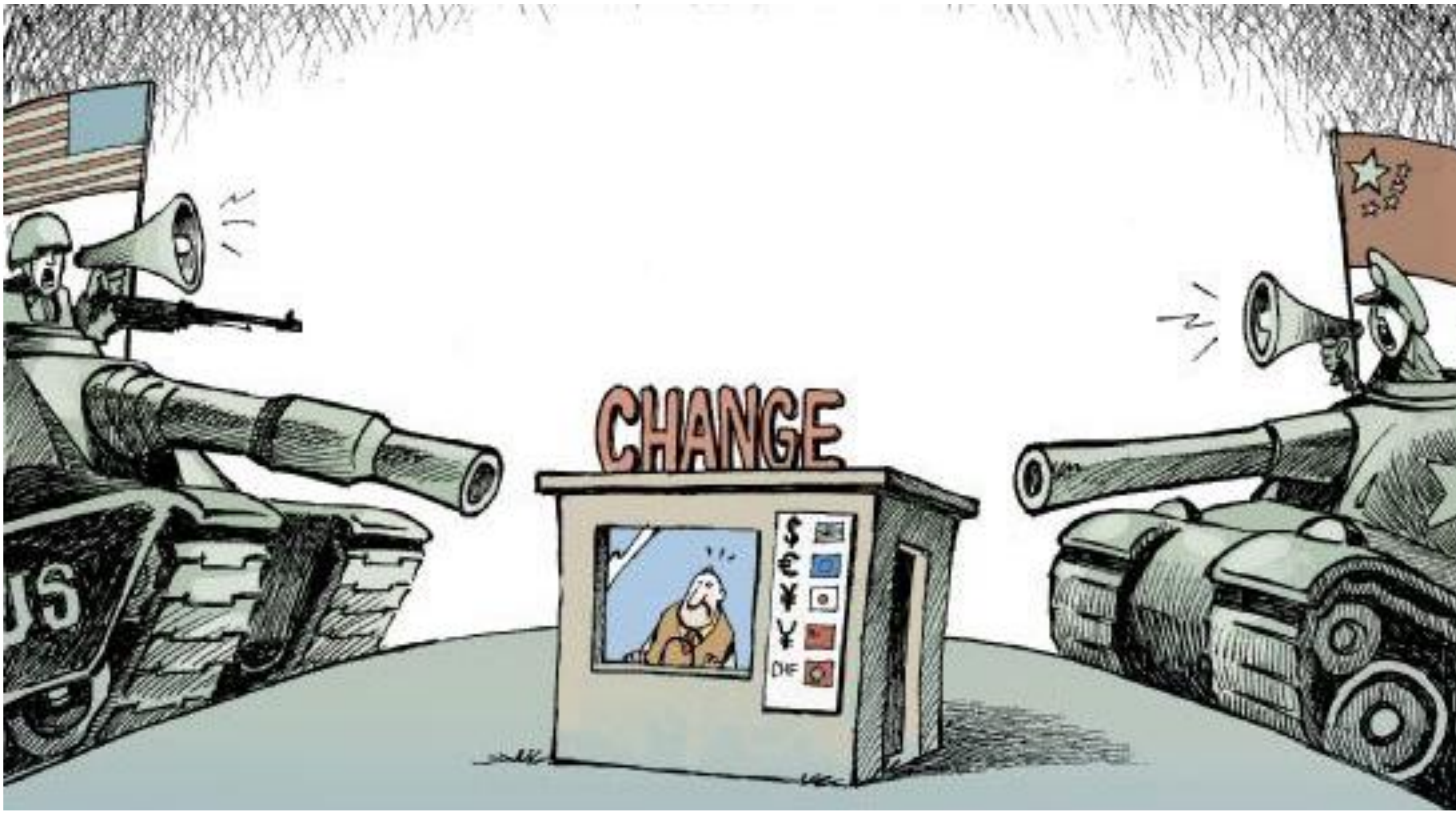
Intellectual property

Doha Negotiations

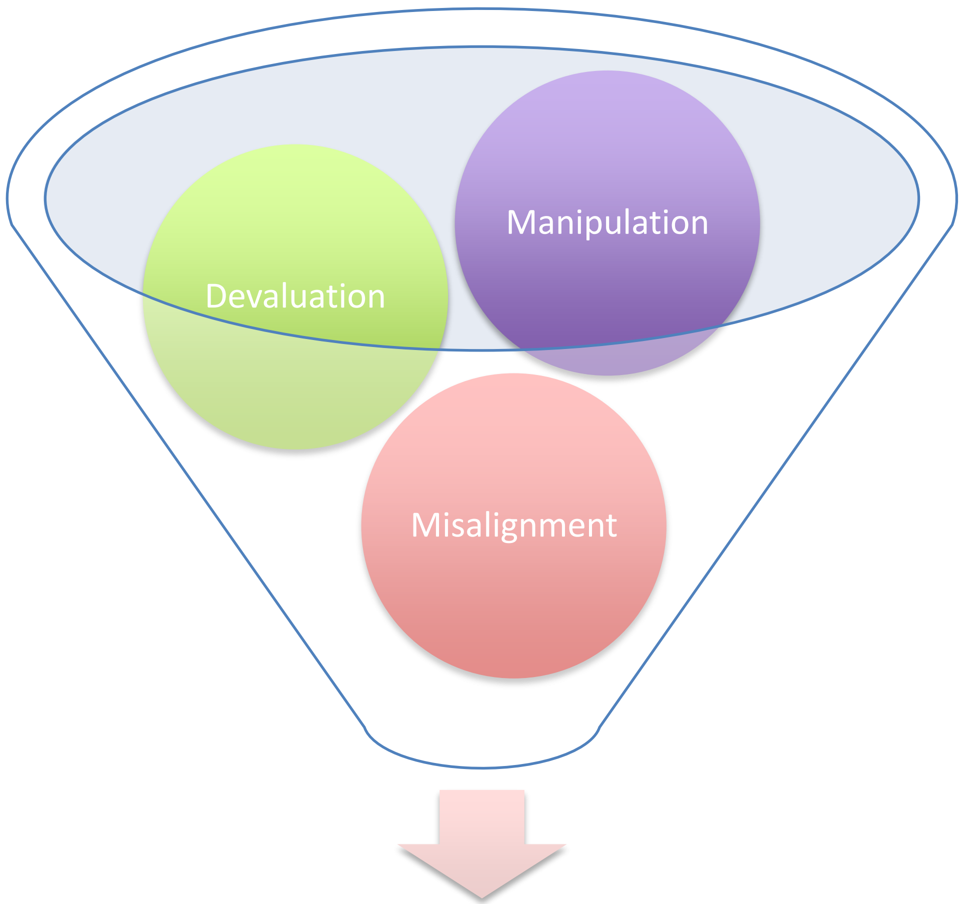
Agriculture

Dispute Settlement

"Currency War"
(Guido *Mantega*, the Brazilian Minister for Finance, 2010)



The terminology conundrum…



Intentional undervaluation of currency to benefit exports

What does it mean?

- Currency manipulation/misalignment/devaluation by countries
- Lowering value of own currency against foreign currency
- Main intention to increase competitiveness and increase exports
- Currency exchange rate used as a tool to increase exports

What constitutes currency misalignment?

- Currency misalignment or manipulation has not been clearly defined in any of the international agreements dealing with trade and currency issues.
- Notion of an “Equilibrium Exchange rate”
- Manipulating the Exchange Rate by deliberate State action to make it move away from the equilibrium

IMF Agreement

Article IV, inter alia, states

"In particular, each member shall: ... avoid manipulating exchange rates or the international monetary system in order to prevent effective balance of payments adjustment or to gain an unfair competitive advantage over other members."

(However, extreme caution has been advised in determination of misalignment and the benefit of any reasonable doubt would be given to the authorities in establishing whether fundamental misalignment is present)

Decision by IMF in 2007

“(a) "Manipulation" of the exchange rate is only carried out through policies that are targeted at—and actually affect—the level of an exchange rate. Moreover, manipulation may cause the exchange rate to move or may prevent such movement.”

“In that regard, a member will only be considered to be manipulating exchange rates in order to gain an unfair competitive advantage over other members if the Fund determines both that: (A) the member is engaged in these policies for the purpose of securing fundamental exchange rate misalignment in the form of an undervalued exchange rate and (B) the purpose of securing such misalignment is to increase net exports.”

G 20 and Currency Wars…

G-20 Communique
Meeting of Finance Ministers and Central Bank Governors
Moscow, 15-16 February 2013

“We reiterate our commitments to move more rapidly toward more market-determined exchange rate systems and exchange rate flexibility to reflect underlying fundamentals, and avoid persistent exchange rate misalignments and in this regard, work more closely with one another so we can grow together.”

Does WTO have a role?

- Is there a trade issue?
- Is there a violation of any of the obligations under WTO Agreements?
- Is there redress under any WTO Agreement?
- Is there a case for a dispute settlement proceeding?

Rumblings of a Currency issue at the WTO

April 2011

- Set in motion by Brazil by submission of a proposal to the Working Group on Trade, Debt and Finance (WGTDF) proposing a debate with a view to better understanding

September 2011

- Another Brazilian proposal highlighting the intricate relationship between exchange rate misalignments and multilateral trade rules – Discussion of possible trade remedies

September 2011

- WTO Secretariat paper on the relationship between exchange rates and international trade

March 2012

- Workshop held at WTO to deliberate on the issue

November 2012

- Brazil initiated another proposal on exchange rates and international trade – existing trade remedies not appropriate to address the issue and new trade remedies required

November 2012

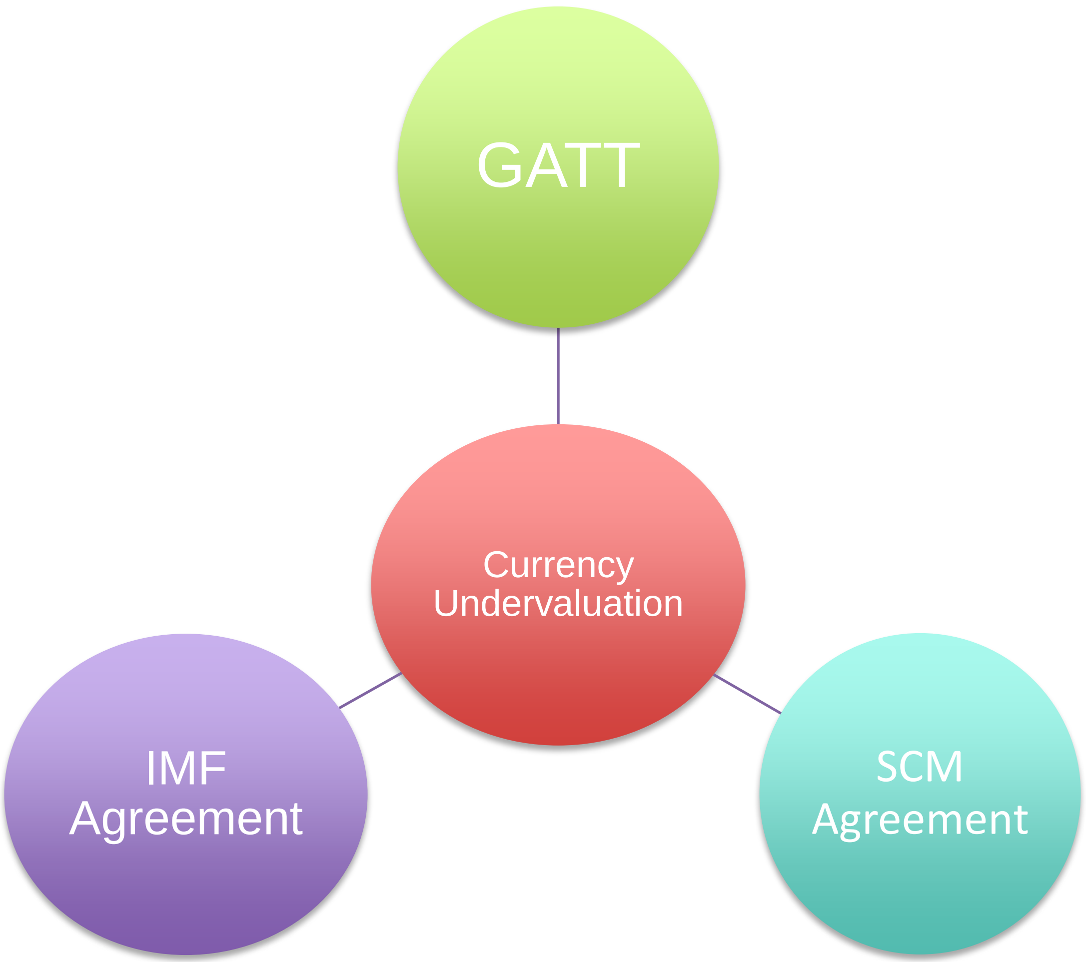
- The WTO seems to be systemically ill-equipped to cope with the challenges posed by the macro and microeconomic effects of exchange rates on trade
- Members may wish, against this background, to consider the need for exchange-rate trade remedies and to start some analytical work to that effect.

China’s reaction to Brazil’s November 2012 proposal

"Currency issue in nature is a monetary policy issue. The right path to resolve this issue is by enhancing the responsibility of and promoting coordination among the international reserve currency issuers.”

(http://www.reuters.com/article/2012/11/26/us-wto-currencies-idUSBRE8AP0XJ20121126)

Currency Undervaluation and compatibility with International Economic Law



WTO provisions involved

General Agreement on Tariffs and Trade

- Article XV GATT – Exchange Arrangements
- Article II GATT – Tariff Commitments

SCM Agreement

- Whether a subsidy under Article I, SCM Agreement
- Whether a prohibited subsidy under Article 3, SCM Agreement

Is Currency Manipulation a violation of WTO obligations?

Violation of Article XV GATT

Article XV (4) GATT

“*Contracting parties shall not, by exchange action, frustrate* the intent of the provisions of this Agreement, nor, by trade action, the intent of the provisions of the Articles of Agreement of the International Monetary Fund.”*

““Ad Article XV

“Paragraph 4

The word “frustrate” is intended to indicate, for example, that infringements of the letter of any Article of this Agreement by exchange action shall not be regarded as a violation of that Article if, in practice, there is no appreciable departure from the intent of the Article.

Relevant terms to interpret…

- What is an Exchange action?
  - Broad interpretation
  - Could include exchange rate policy

- What amounts to “frustrate”
  - make ineffectual", "counteract" or "invalidate”
  - “prevention of success or fulfillment”

- “the intent of the provisions”
  - Not all provisions

Article XV (4) of the GATT definitely offers an opportunity to the critics of currency misalignment to attempt a legal challenge at the dispute settlement forum. That the provision has not been tested or interpreted may not be reason enough for the claim not to succeed.

Violation of Article II GATT commitments

- Article II of the GATT is one of the basic provisions of the multilateral trading system. It lays down the tariff concessions that a country is bound to under the international rules.

"*1. (a) Each contracting party shall accord to the commerce of the other contracting parties treatment no less favourable than that provided for in the appropriate Part of the appropriate Schedule annexed to this Agreement.*"

- When tariff concessions are bound the duties assessed on the bound items may not be greater than the bound rate.

- Bindings give legal assurance that tariffs will not be raised beyond the maximum tariff level.

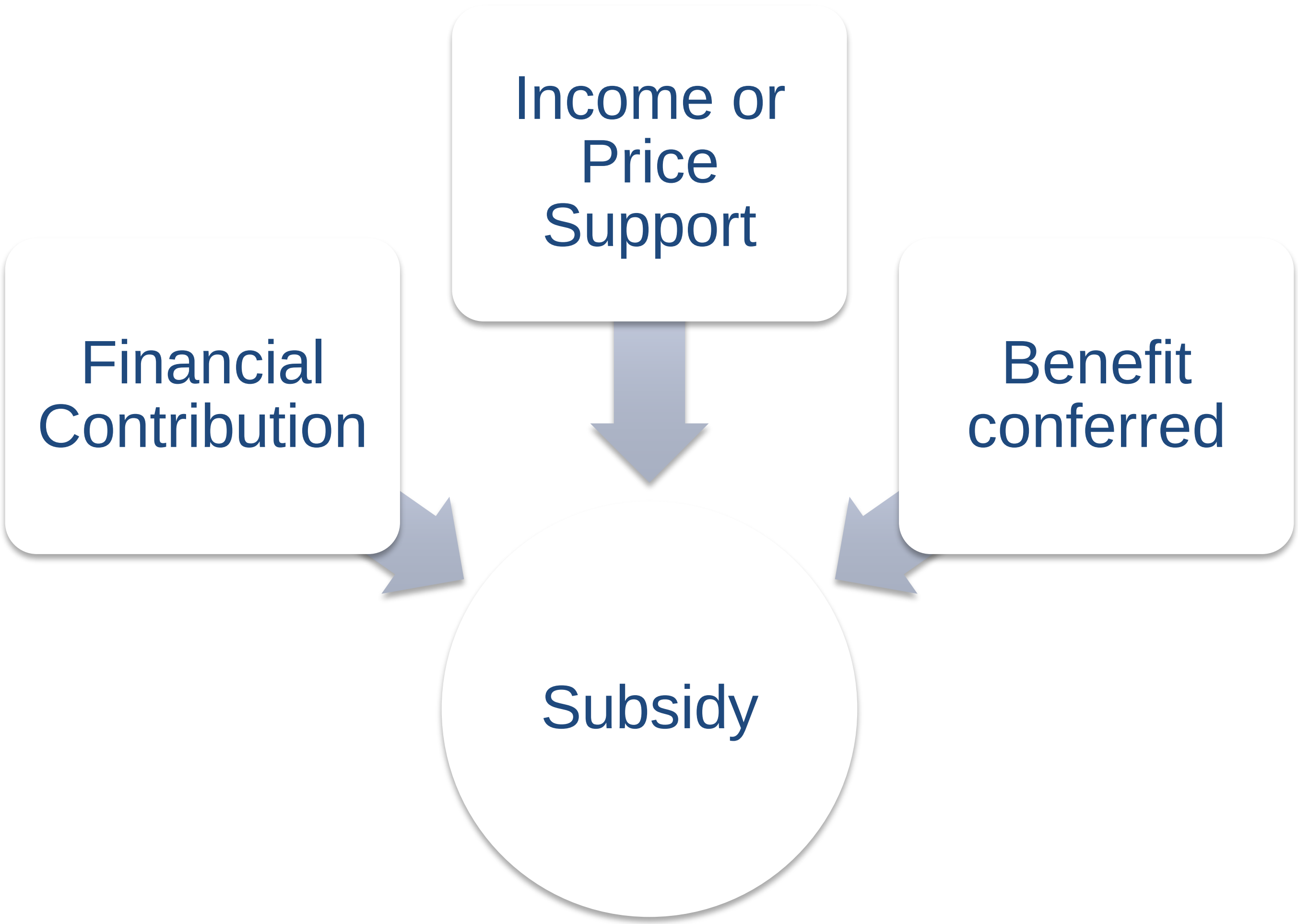
Article II GATT continued…

Currency misalignments may result in the actual tariff being much higher or lower than the bound rate of tariffs as per the schedule of commitments.

By a “tariffication” exercise, ndervaluation of a currency may lead to the applied rate crossing the bound rate

Currency undervaluation could upset a country’s tariff bindings pursuant to Article II of the GATT

Violation of SCM Agreement?



Whether it is a subsidy contingent on exports under Article 3 ASCM?

Financial contribution…

(a)(1) there is a financial contribution by a government or any public body within the territory of a Member (referred to in this Agreement as "government"), i.e. where:

(i) a government practice involves a direct transfer of funds (e.g. grants, loans, and equity infusion), potential direct transfers of funds or liabilities (e.g. loan guarantees);"

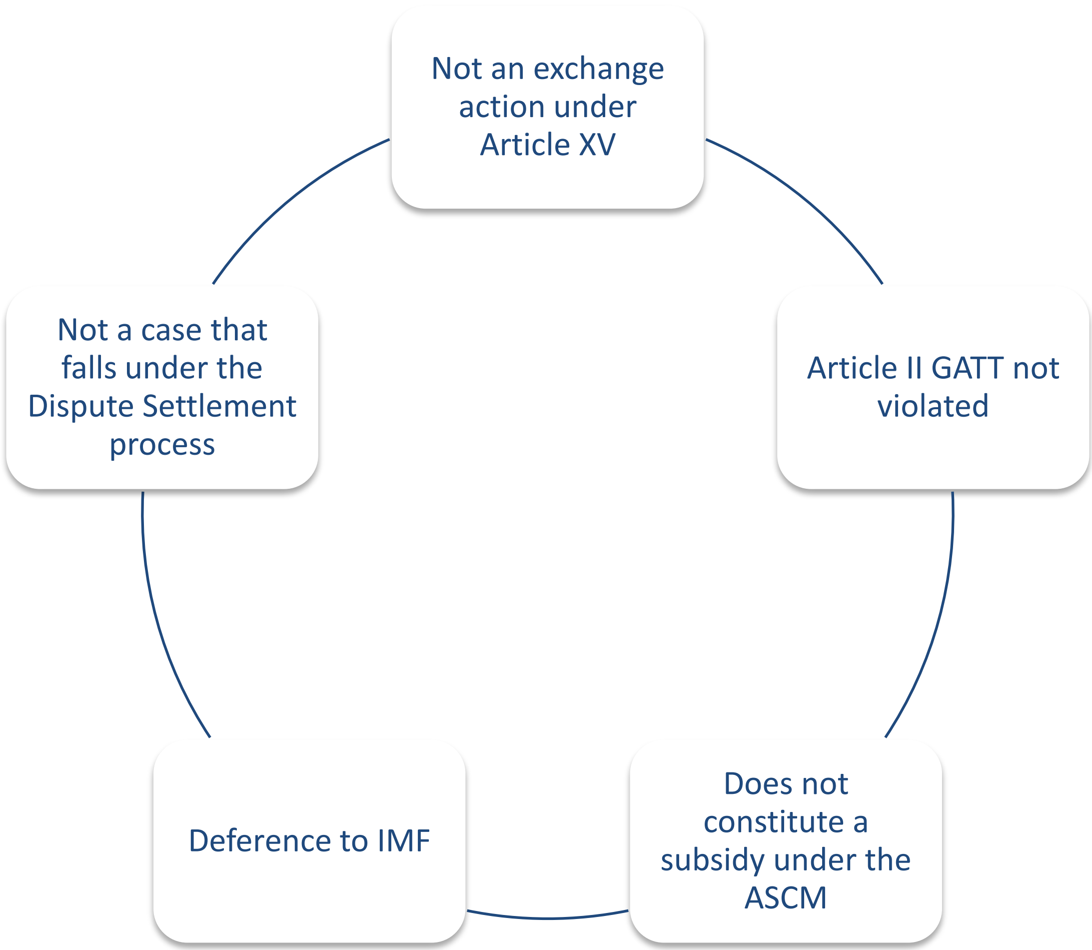
“Prohibited subsidy” under the SCM Agreement ?

Article 3.1- Subsidies within the meaning of Article 1, shall be prohibited:

(a) subsidies contingent, in law or in fact, whether solely or as one of several other conditions, upon export performance…

Currency misalignment policy is also seen as constituting a “financial contribution: conferring a “benefit to the exporters” and “contingent on exports” and are viewed as being incompatible with the provisions of the ASCM.

Currency Manipulation – No WTO violation?

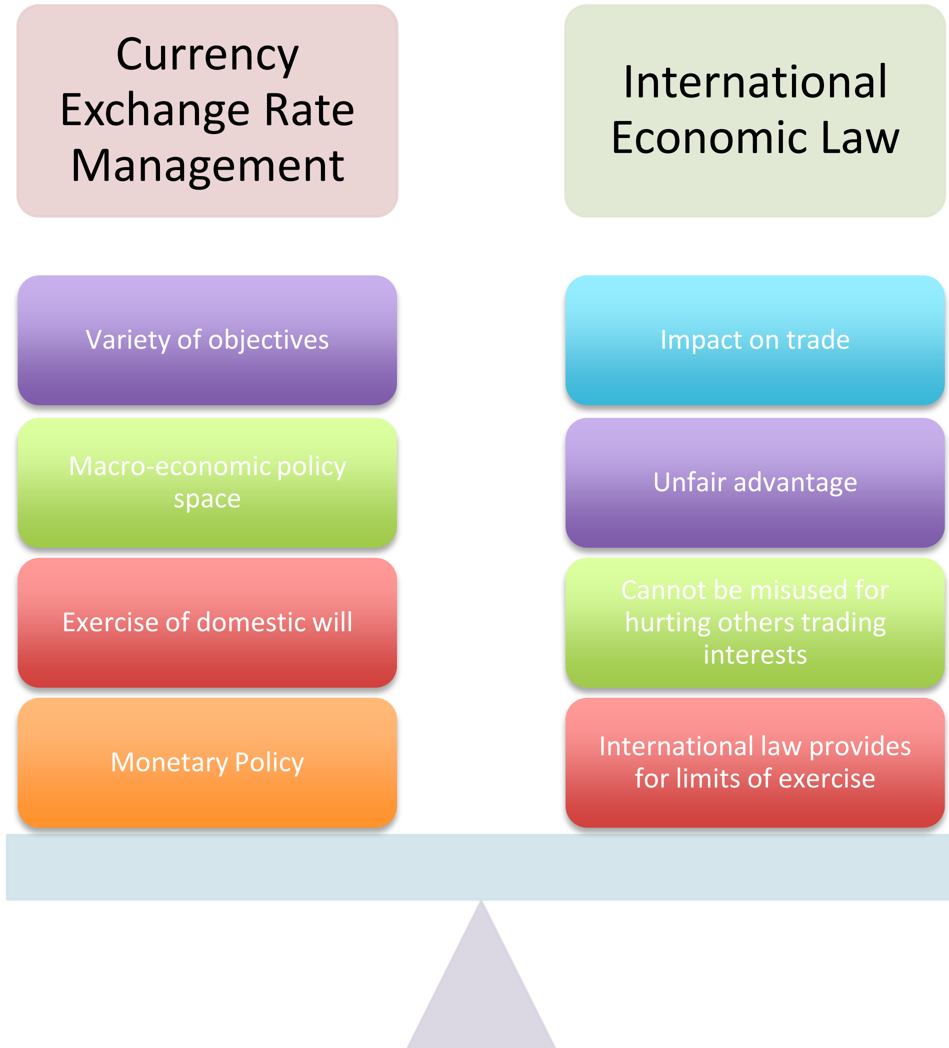


Issue of the Right Forum…

IMF is the legitimate international institution to address currency exchange rate issues

WTO has the strength of the dispute settlement process that ensures enforceable decisions

Currency manipulation and domestic policy space



Complexities and concerns…

- Monetary policy complexity – Thin line between exercise of domestic monetary policy and exchange rate manipulation
- Complex econometric models and macro-economic policy issues
- No unanimity on what constitutes “currency manipulation” as well as whether impacts trade at all

Recent developments…

US Auto industry and currency manipulation in TPP
9th January 2014

(http://www.youtube.com/watch?v=r2kv37S3Sn4)

“Given the interconnection between trade and finance, to achieve an ambitious result, the trade pact must ensure that currency manipulation by a TPP member does not frustrate the market access commitments set forth in the final agreement.

…

The American Automotive Policy Council, on behalf of its members, Chrysler, Ford and General Motors, calls for the inclusion of strong, enforceable currency provisions in the Trans-Pacific Partnership (TPP) Agreement.”

Bipartisan Trade Promotion Authorities Bill 2014

PRINCIPAL TRADE NEGOTIATING OBJECTIVES

“(11) CURRENCY.—The principal negotiating objective of the United States with respect to currency practices is that parties to a trade agreement with the United States avoid manipulating exchange rates in order to prevent effective balance of payments adjustment or to gain an unfair competitive advantage over other parties to the agreement, such as through cooperative mechanisms, enforceable rules, reporting, monitoring, transparency, or other means, as appropriate.”

Currency manipulation provisions in trade agreements

Demand by domestic policy makers
Letter of 230 US House of Representative members – June 2013

"Undervalued exchange rates allow other countries to boost exports of their products and impede exports of ours.

…

Including currency disciplines in the TPP is consistent with and will bolster our ongoing efforts to respond to these trade-distorting policies.

Congress of the United States
Washington, DC 20515

June 6, 2013

President Barack Obama
The White House
Washington, D.C. 20500

Dear President Obama:

As the United States continues to negotiate the Trans-Pacific Partnership, it is imperative that the agreement address currency manipulation. Exchange rates strongly influence trade flows, and, in recent years, currency manipulation has contributed to the U.S. trade deficit and cost us American jobs. Incorporating currency provisions in the agreement will strengthen our ability to combat these unfair trade practices and help to create a level playing field for American workers, businesses, and farmers.

Undervalued exchange rates allow other countries to boost exports of their products and to impede exports of ours. They also contribute to trade imbalances and market access limitations that make it difficult for U.S. companies to compete in foreign countries. According to the Peterson Institute for International Economics, a minimum of one million American jobs have been shipped overseas as a result of currency manipulation alone. The consequences are not singular to the U.S.; misaligned currencies are distorting the entire global economy.

Despite U.S. efforts to address currency manipulation at the G-20, major currencies remain significantly undervalued. Including currency disciplines in the TPP is consistent with and will bolster our ongoing efforts to respond to these trade-distorting policies. It will also raise TPP to the 21st century agreement standard set by the Administration. More importantly, it will create a level playing field for American businesses and workers and prevent more U.S. jobs from being shipped overseas.

Thank you for your consideration of this letter. We look forward to working with you to address undervalued exchange rates in the TPP agreement.

Sincerely,

MICHAEL H. MICHAUD
Member of Congress

SAM GRAVES
Member of Congress

JOHN D. DINGELL
Member of Congress

RICK CRAWFORD
Member of Congress

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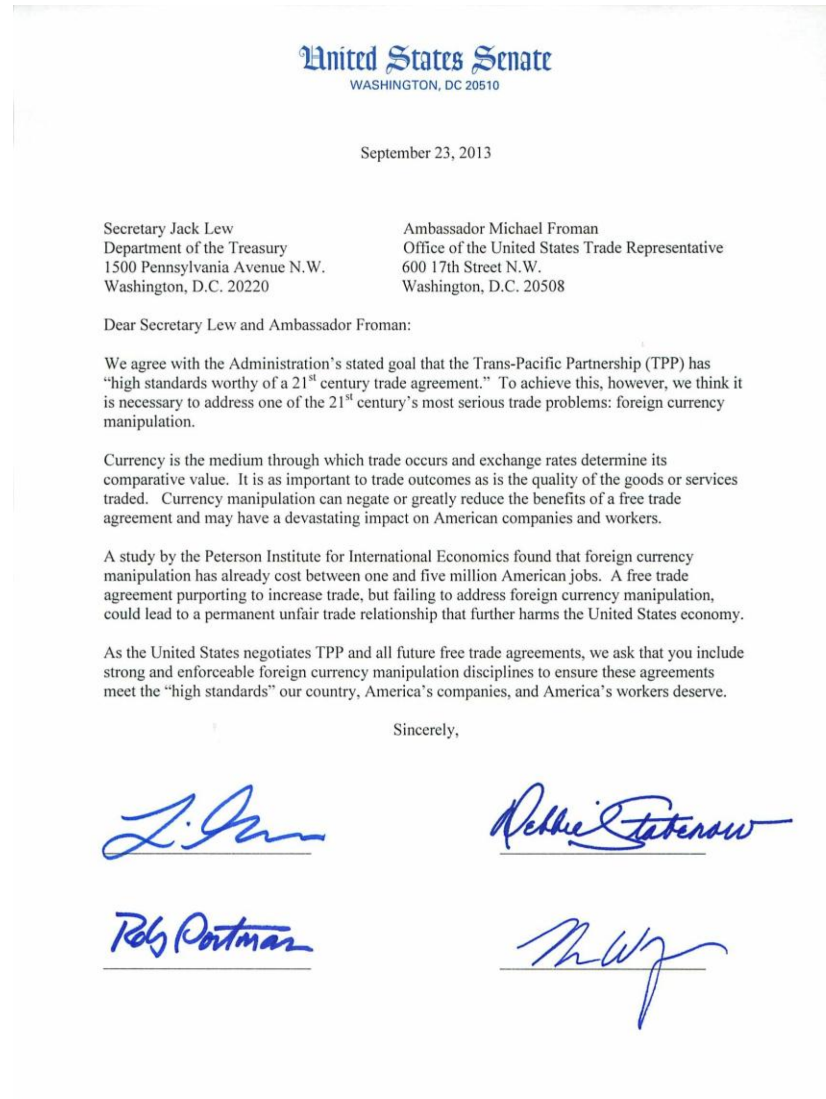
Currency manipulation provisions in trade agreements

Demand by domestic policy makers
Letter of 60 US Senators – September 2013

“Currency manipulation can negate or greatly reduce the benefits of a free trade agreement and may have a devastating impact on American companies and workers.”

…

As the United States negotiates TPP and all future free trade agreements, we ask that you include strong and enforceable foreign currency manipulation disciplines to ensure these agreements meet the "high standards" our country”



United States Senate
WASHINGTON, DC 20510

September 23, 2013

Secretary Jack Lew
Department of the Treasury
1500 Pennsylvania Avenue N.W.
Washington, D.C. 20220

Ambassador Michael Froman
Office of the United States Trade Representative
600 17th Street N.W.
Washington, D.C. 20508

Dear Secretary Lew and Ambassador Froman:

We agree with the Administration’s stated goal that the Trans-Pacific Partnership (TPP) has “high standards worthy of a 21st century trade agreement.” To achieve this, however, we think it is necessary to address one of the 21st century’s most serious trade problems: foreign currency manipulation.

Currency is the medium through which trade occurs and exchange rates determine its comparative value. It is as important to trade outcomes as is the quality of the goods or services traded. Currency manipulation can negate or greatly reduce the benefits of a free trade agreement and may have a devastating impact on American companies and workers.

A study by the Peterson Institute for International Economics found that foreign currency manipulation has already cost between one and five million American jobs. A free trade agreement purporting to increase trade, but failing to address foreign currency manipulation, could lead to a permanent unfair trade relationship that further harms the United States economy.

As the United States negotiates TPP and all future free trade agreements, we ask that you include strong and enforceable foreign currency manipulation disciplines to ensure these agreements meet the “high standards” our country, America’s companies, and America’s workers deserve.

Sincerely,

Debbie Stabenow

Rob Portman

What next?...

- Who will fire the first bullet?
- Does the Dispute Settlement Understanding prevent filing of a case under the WTO?
- Will a Member file a WTO case or initiate domestic CVD investigation against another “manipulator” Member?
- Will there be more discussion in the WTO Committees/Councils?
- Will it be covered in a Free Trade Agreement?
- Will there be a move towards a new international legal or policy framework?

Will “currency manipulation” be the next big trade dispute in this decade at the WTO?

(http://www.youtube.com/watch?v=zOtYkrwr2UE)

Thank You

Srikar.M.S.
Director, Trade Policy Division,
Department of Commerce
Government of India