

U.S. Foreign Exchange Policy

Currency Provisions and Trade Deals

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The Barack Obama administration's efforts to secure Trade Promotion Authority (TPA), in conjunction with advancing the Trans-Pacific Partnership (TPP), brought into focus a congressional push to associate currency provisions with U.S. trade agreements. Since that time, discussions on the association of currency provisions with trade deals have gained momentum and become a feature of U.S. foreign exchange policy, especially under the Donald Trump administration. *What is the historical context for including currency provisions alongside or as part of trade deals in U.S. exchange rate policy? What has actually been done? Is including currency provisions alongside or in trade deals a good idea? How should this be best managed?*¹

KEY POINTS

- There is a decades-long history in the United States of perceptions about unfair foreign currency practices and/or excessive reliance on the U.S. economic engine to fuel global growth, giving rise to protectionist pressures.
- Often, U.S. currency complaints have been legitimate. But currency market pressures have also been an unintended product of U.S. policies—especially excessively expansionary fiscal policy—a reality U.S. officials are loath to admit.
- Republican and Democrat administrations until the present sought to make progress on currency issues, while managing and defusing currency-related protectionist pressures. These realities have been reflected in the evolution of the U.S. Treasury's Foreign Exchange Reports, as well as U.S.-led initiatives in multilateral fora such as the Group of 7 (G-7); Group of 20 (G-20); and the International Monetary Fund (IMF).
- The Trump administration has loudly complained about unfair currency practices and actively sought to bring exchange rate issues into trade deals.

1. Thanks to John Weeks and Stephanie Segal for helpful and insightful comments.

- To date, several different approaches for managing currency provisions in association with trade deals have emerged. For the TPP, a joint declaration of macroeconomic authorities separate from the trade deal was developed. The amended U.S.-Korea Free Trade Agreement (KORUS) deal only reached currency understandings, which are not published. The United States-Mexico-Canada Agreement (USMCA), signed in November 2018, includes currency provisions inside the agreement, marking the first time certain foreign exchange policy commitments would be legally enforceable and setting a precedent for the future.
- Rendering judgments about currency values and movements is inherently complex. There is no agreed methodology for precisely measuring equilibrium exchange rates and under- and overvaluation. There are technical questions about what exchange rate to look at—trade-weighted or bilateral—how to calculate such rates, and how to apportion responsibility for a given currency development and movement, since currency valuation is relative.
- Further, current account positions—a basis for any assessment of currency “under-” or “overvaluation”—are structurally rooted in an economy’s saving and investment decisions. Often, fiscal and monetary policies drive capital flows and exchange rate movements, and capital flows can swamp trade flows. Country authorities, especially independent central banks, will not subordinate domestic objectives to an external discipline.
- Treasury has had to grapple with these inherent complexities over the years. This has frequently led to congressional frustration with Treasury.

Including currency provisions in or alongside trade deals has many undesirable drawbacks. Ideally, they would not be included. Foreign countries, though, should reluctantly accept the U.S. political reality that currency issues may need to be associated with trade negotiations. Hence, efforts should focus on sensibly managing outcomes. Transparency is essential, in contrast to the unpublished understandings in the revised KORUS deal, which is thus not likely a sustainable model. Foreign and U.S. authorities should avoid hubris in discussing currency provisions. Such provisions should not constrain macroeconomic policy in pursuing domestic objectives. Foreign exchange issues should not be subject to dispute resolution. Rather, they should be left to discussions among macroeconomic authorities and not be inside trade deals. Given the political inevitability that currency provisions will be associated with trade deals, the TPP Joint Declaration approach is the best of the highly imperfect options.

Brief Historical Context

Debates about exchange rates and their implications for U.S. economic performance and the trade deficit have been rife in U.S. political discourse, especially since the early 1970s with the breakdown of the Bretton Woods System and the advent of more flexible exchange rate regimes in advanced economies. The U.S. debate has often been associated with perceptions of unfair trading practices by major U.S. trading partners and frequent recourse to protectionist pressures, especially in Congress. U.S. administrations from both parties have also long expressed concerns about excessive global reliance on the United States as the importer of first and last resort. The debate over trade and trade policy is also infused by societal angst over technological change, globalization, and growing inequality.

While technological change and globalization have altered U.S. employment and production patterns, movements in the U.S. dollar and exchange rates often receive significant—and at times more—attention. More generally, fluctuations in the U.S. dollar have sometimes been large in both directions, impacting relative trade competitiveness. Further, currency swings can undermine expected gains from trade agreements.

A brief historical overview helps contextualize today's debates.² In the mid-1960s, the Lyndon Johnson administration pursued guns and butter to pay for the Vietnam War and the Great Society. Inflation and the budget deficit in the United States surged. Global confidence in the U.S. dollar was undermined. Efforts by global central banks to shore up gold convertibility into the U.S. dollar came under stress. While the rest of the world felt the United States was behaving imprudently, many at home pointed to foreigners imposing excess burdens on the United States and failing to adjust. Protectionist pressures emerged. In August 1971, President Richard Nixon unilaterally imposed a 10 percent across-the-board import surcharge and suspended U.S. dollar convertibility, meaning the U.S. dollar would no longer be convertible into gold in international markets. His colorful Secretary of the Treasury, John Connally, was famously quoted around the time—"My philosophy is that all foreigners are out to screw us, and it's our job to screw them first." In another pithy quote, he told a group of European Finance Ministers, the "dollar is our currency, but your problem."

U.S. macroeconomic performance in the 1970s was characterized by high inflation. In late 1979, Federal Reserve Chair Paul Volcker engineered a massive tightening of liquidity to wring out persistent inflation. In the early 1980s, President Ronald Reagan adopted a supply-side tax cut and ramped up military spending. A bloated budget deficit emerged. The mix of tight monetary policy and expansionary fiscal policy further sent interest rates soaring. Recession ensued. Unsurprisingly, the U.S. dollar appreciated sharply, and the U.S. trade deficit rose. Soon the Midwest became known as the "Rust Belt." With enormous protectionist pressure mounting, Treasury Secretary James Baker launched the Plaza Accord in 1985 to coordinate foreign exchange market intervention among the United States, United Kingdom, France, Germany, and Japan. The accord helped weaken the U.S. dollar.

In the mid-2000s, the U.S. current account deficit rose to nearly 6 percent of GDP. Much of the counterpart found itself in China's current account surplus, which soared toward 10 percent of GDP, with the renminbi (RMB) essentially pegged to the U.S. dollar amid massive reserve accumulation. The increase in the surplus also followed China's accession into the World Trade Organization in 2001. Many U.S. manufacturers pointed to Chinese currency practices as hollowing out their industries. Protectionist forces in the United States resurfaced with a vengeance, epitomized by the Schumer-Graham bill, which would have slapped a 27.5 percent tariff on Chinese goods entering the United States. Despite massive bilateral efforts by the United States to engage China to appreciate the RMB, and despite some success as early as 2005, these efforts were deemed too little too late and insufficient.

In 2018, the U.S. dollar appreciated across the board, including against the RMB, as the Federal Reserve moved interest rates higher as part of normalization and the U.S. economy grew strongly on the back of a pro-cyclical fiscal policy due to the 2017 Tax Cuts and Jobs Act. This appreciation reinforced administration views about RMB and euro currency manipulation.

In general, the rest of the world views the U.S. dollar's role in the international monetary system as providing the United States with an "exorbitant privilege."

Indeed, the U.S. dollar's role conveys important benefits, including that the world's continued demand for U.S. dollar liabilities means the United States does not face the same financing constraints as other countries. But the U.S. dollar's role also has been associated with excess global reliance on U.S. demand and persistent and larger U.S. external deficits than would otherwise be the case—what some have called

2. Mark Sobel, OMFIF, "U.S. International Financial Diplomacy – Past, Present, and Future," January 30, 2019, https://www.omfif.org/media/5508834/us-financial-diplomacy-mark-sobel-speech_-220119-2.pdf.

the U.S. dollar’s “indestructible curse.” One thing is clear, while the United States may have had at times legitimate concerns with others’ currency practices, U.S. macroeconomic policies have frequently been sub-optimal—fiscal policy in particular—and drove some of the very currency market outcomes that fostered protectionist pressures.

What Has Been Done?

The political pressures surrounding foreign exchange developments in the early and mid-1980s resulted in the 1988 Omnibus Trade and Competitiveness Act. This act mandated Treasury to prepare the semi-annual reports on “Macroeconomic and Foreign Exchange Policies of Major Trading Partners of the United States”—better known as the FX Report.³

The 1988 legislation mandated that the Treasury examine the foreign exchange practices of major U.S. trading partners and determine whether countries “manipulated” their currencies against the U.S. dollar for purposes of preventing effective balance of payments adjustments or gaining unfair competitive advantage in international trade. If so, Treasury was required to undertake expedited bilateral negotiations with the concerned country to remedy the situation. Between 1988 and 1994, several countries were designated for such currency practices, often relating to multiple currency practices, but no country has been designated since then.⁴

In the mid-2000s, as issues arose with China (see above), extensive discussions took place between the Treasury and Congress on possible new legislation to revise the requirements of the FX Report. But an agreement was not reached, as the George W. Bush administration did not support the Schumer-Graham bill. Other currency bills were floated allowing for countervailing duties to be imposed for currency undervaluation or manipulation, which the administration also pushed back against.⁵ Treasury also was required to meet several reporting requirements to Congress, including on clarifying the statutory definition of currency “manipulation.”⁶

The drive for currency legislation abated, though, with the onset of the Global Financial Crisis (GFC). The U.S. dollar fell sharply in currency markets during the GFC, especially as the Federal Reserve cut interest rates to the zero lower bound ahead of European central banks and then engaged in quantitative easing (QE). Indeed, some nations—led by Brazil’s Finance Minister who coined the term “currency wars”—alleged that the Federal Reserve was intentionally devaluing the U.S. dollar to gain a U.S. competitive edge. China’s current account surplus, which peaked at 10 percent of GDP, also fell sharply.

But in 2013, Congressional attention to exchange rate developments picked up anew. Chinese foreign exchange reserves were rising sharply. Japan enhanced its quantitative easing, and some Japanese officials publicly framed the effort in terms of depreciating the yen and boosting exports. Others even advocated purchasing foreign assets (e.g., intervening in currency markets) to do so. Needless to say, U.S. automakers protested loudly.

3. “Macroeconomic and Foreign Exchange Policies of Major Trading Partners of the United States,” U.S. Department of the Treasury, 2018, <https://home.treasury.gov/policy-issues/international/macroeconomic-and-foreign-exchange-policies-of-major-trading-partners>.

4. U.S. Department of the Treasury, “Appendix 2: Past U.S. Treasury Determinations with Respect to Economies Considered to Have Manipulated Their Exchange Rate,” Resource Document, 2018, <https://www.treasury.gov/resource-center/international/exchange-rate-policies/Documents/appendix2finalapril152009.pdf>.

5. U.S. Department of the Treasury, “Currency Views Letter,” Resource Document, July 30, 2007, <https://www.treasury.gov/press-center/press-releases/Documents/currencyviewsletter.pdf>.

6. U.S. Department of the Treasury, “Report to the Committees on Appropriations on Clarification of Statutory Provisions Addressing Currency Manipulation,” Press Release, 2005, <https://www.treasury.gov/press-center/press-releases/Documents/js2308.pdf>.

In February 2013, the United States pressed the G-7 Finance Ministers to put forward new currency language and then worked to incorporate as much of the language as possible in G-20 communiqués. The heart of the G-7 language was to insist that economic policy would remain oriented toward achieving domestic objectives using domestic instruments, and not to target exchange rates. The February 2013 G-20 Finance Ministers language emphasized more rapid movement toward market-determined exchange rates and flexibility, avoiding persistent misalignments, not targeting exchange rates for competitive purposes and refraining from competitive devaluation.

Lengthy discussions occurred on currency issues as part of the negotiations between the Obama administration and Congress to renew the TPA. The TPA was a necessary precursor to the TPP, and it passed Congress in April 2015. Congress included language in the TPA bill stating that: “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.”⁷ This language for the first time formally associated currency issues with trade agreements.

In conjunction with the TPA language, U.S. Treasury officials began talks with TPP participants on macroeconomic and currency issues. Other TPP members were highly opposed to including currency and especially any enforceable currency disciplines.

In the end, TPP partners compromised given the need to include the United States, agreeing on a “Joint Declaration of the Macroeconomic Policy Authorities of the Trans-Pacific Partnership.” The Joint Declaration, agreed in November 2015, reflected those tensions.⁸ It is legally separate from the TPP agreement itself. In particular, it mirrors views among many participants that analyzing and assessing relative currency movements and misalignments is an inherently complex undertaking fraught with hurdles.

But the declaration did reaffirm participants’ agreement to abide by the new G-20 exchange rate language; commit participants to useful requirements for increased transparency on macroeconomic policies, foreign exchange market intervention, and other balance-of-payments developments; and require at least once-a-year macroeconomic consultations among TPP participants.

In addition, in early 2016, Congress passed the “Trade Facilitation and Trade Enforcement Act of 2015.” It included a section on engagement on exchange rate and economic policies, seeking to reduce Treasury’s discretion and promote a more quantified and less qualitative focus in the FX Reports on identifying currency “manipulation.” That section reflected an amendment by Senators Michael Bennet, Orrin Hatch, and Tom Carper—the so-called “Bennet Amendment.”

The legislation requires Treasury to conduct “enhanced analysis” of major trading partner currency practices. In response, Treasury now has developed a more focused three-part test for identifying major partner currency practices than existed in the preparations of the FX Report pursuant to the 1988 act. This test entails a more quantitative discussion of whether major trading partners have: (1) a significant

7. U.S. Congress, Senate, *Bipartisan Congressional Trade Priorities and Accountability Act of 2015*, S 995, 114th Cong., 1st sess., introduced in Senate April 16, 2015, <https://www.govinfo.gov/content/pkg/BILLS-114s995rs/pdf/BILLS-114s995rs.pdf>.

8. Policy Authorities for Countries to the TPP, “Joint Declaration of the Macroeconomic Policy Authorities of Trans-Pacific Partnership Countries,” U.S. Department of the Treasury, November 20, 2015, [https://www.treasury.gov/initiatives/Documents/TPP_Currency_November 2015.pdf](https://www.treasury.gov/initiatives/Documents/TPP_Currency_November%202015.pdf).

bilateral trade surplus with the United States, (2) a material global current account surplus, and (3) engaged in persistent, one-sided intervention in the foreign exchange market.⁹

No country has yet to run afoul of all three parts of the test. Countries that run afoul of two are put on a “monitoring list”—unless that country is China, which then uniquely has the good fortune to be included on the basis of tripping one of the three given that it “accounts for a large and disproportionate share of the overall U.S. trade deficit.”

In terms of consequences under the 2015 act, the administration—somewhat similar to the 1988 act—is required to commence enhanced bilateral engagement with any country that meets all three criteria. Of course, U.S. financial diplomats in any case engage countries extensively on their currency practices, regardless of whether they meet all three criteria. Additionally, the 2015 act specifies some remedial actions, none of which on their face would appear to be very consequential.¹⁰

While the quantitative focus is useful, Treasury’s execution of the 2015 act has altered the FX Report in other ways. The report now focuses more granularly on the three-part test, limiting a richer discussion for the public of global economic developments. The three parts are weighted equally, whereas economists dismiss the relevance of bilateral balances, and a country can perversely be put on the monitoring list, even when it has a current account deficit. China remains on the monitoring list despite its current account surplus having largely gone away and not accumulating reserves for several years. Only 12 major trading partners are included, whereas bringing in the top 20 could highlight trading partners that do raise legitimate questions about currency practices and are still rather significant.¹¹

President Trump has loudly complained about “currency manipulation” and attached great weight to reducing U.S. bilateral trade deficits. Accordingly, the push to include currency provisions in trade agreements has gained more momentum under his administration.

As part of the amended KORUS deal, signed in September 2018, the administration declared it was working to ensure that U.S. goods were treated fairly and that U.S. trading partners avoided unfair currency practices. To that end, and separate from KORUS, Treasury reached an understanding with South Korea’s Ministry of Economy and Finance to avoid competitive devaluation and practices providing for an unfair competitive advantage; the understanding included “strong commitments on exchange rate practices, robust transparency and reporting.”¹²

Despite the president’s stated commitment to “robust transparency,” the “understanding” curiously has not been published. Surely, Congress and the public should ask why. Regardless, a few observations may be noted.

- South Korea (ROK) long ago signed off on the G-20 currency commitments reached in February 2013 and repeatedly reaffirmed since then. These G-20 commitments are general in nature.

9. U.S. Department of the Treasury Office of International Affairs, *Foreign Exchange Policies of Major Trading Partners of The United States* (U.S. Department of the Treasury Office of International Affairs, 2016), 13-29.

10. (1) Denying access to OPIC financing; (2) excluding the country from U.S. government procurement; (3) calling for heightened IMF surveillance; and (4) instructing the United States Trade Representative to take into account such failure to adopt appropriate policies in assessing whether to enter into a trade agreement or initiate or participate in trade agreement negotiations. The president may waive the remedial action requirement under specified circumstances.

11. Mark Sobel, “Augmenting US Treasury Foreign Exchange Report,” OMFIE, February 19, 2019, <https://www.omfif.org/analysis/commentary/2019/february/augmenting-treasury-trade-partner-report/>.

12. Donald J. Trump, “President Donald J. Trump Is Fulfilling His Promise on the United States–Korea Free Trade Agreement and on National Security,” White House, September 24, 2018, <https://www.whitehouse.gov/briefings-statements/president-donald-j-trump-fulfilling-promise-united-states-korea-free-trade-agreement-national-security/>.

- ROK recently committed to enhanced transparency on its foreign exchange operations and will now report on its intervention. This is to be strongly welcomed, although direct intervention (including through swaps) is but one way of influencing currency movements.
- But ROK has long been a problematic case of a country with a large current account surplus, an undervalued currency, and frequent foreign exchange market intervention. Enhanced transparency need not change those realities. While ROK has intervened to buy and sell U.S. dollars in response to ups and downs, respectively, in its currency, this intervention has been asymmetric—ROK has acted much more forcefully to curb appreciation of its currency, rather than depreciation.

Around this time, the United States, Mexico, and Canada reached agreement on the so-called USMCA trade deal—NAFTA 2.0. This deal includes commitments to market-determined exchange rates and adherence to the IMF Articles of Agreement strictures against currency manipulation. Chapter 33's transparency and reporting requirements call for public disclosure of monthly data on international reserve balances and intervention in foreign exchange markets as well as the quarterly balance of payments data.

It also establishes a Macroeconomic Committee among the three countries that will meet at least annually to monitor implementation, allowing any of the three to initiate bilateral consultations should the policies and measures of another be seen as violating policy and reporting commitments. Finally, the parties can make use of dispute resolution for any perceived failure to meet transparency and reporting obligations but not for exchange market intervention or alleged currency manipulation.¹³

What is novel about the USMCA currency provisions is that they are included within the USMCA itself. Recall that the TPP “Joint Declaration” was separate from the actual TPP deal. The currency provisions under the amended KORUS deal were just an “understanding.” A few observations are in order:

- The United States, Canada, and Mexico allow their exchange rates to float freely and in essence, do not intervene in exchange markets.
- Thus, assertions about “currency manipulation,” “competitive depreciation,” “gaining unfair competitive advantage and preventing effective balance of payments adjustment” ring hollow for USMCA.
- All three long ago signed up to G-20 currency commitments (and the United States and Canada to G-7 commitments as well).
- All three are highly transparent about reserves, intervention data, and macroeconomic policy more generally.
- The three countries monitor each other's policies and markets closely and have multiple bilateral and multilateral opportunities to engage.

Thus, while the USMCA currency provisions are not going to impact the currency policies of the three countries, the inclusion of the USMCA currency provisions inside the trade agreement will be significant if it has precedential value for other trade deals. In that light, the lack of inclusion of currency provisions inside the amended KORUS agreement and the use of un-transparent “understandings”—given that ROK has long pursued questionable currency practices and that KORUS discussions were broadly taking place around the same time as USMCA—is perplexing.

13. Stephanie Segal, "USMCA Currency Provisions Set a New Precedent," Center for Strategic and International Studies (CSIS), October 5, 2018, <https://www.csis.org/analysis/usmca-currency-provisions-set-new-precedent>.

The Trump administration has recently stated that an agreement on the stability of the RMB has already been reached with China as part of the U.S.-China trade talks. It has yet to be seen what the nature and form of the agreement is—is it a part of the “deal;” does it have legal force; what precisely does it commit China to do; and are there associated U.S. commitments? Regardless, China has sought to curb downward RMB pressures over the last year, RMB depreciation in 2018 was more a reflection of a rising U.S. dollar than falling RMB, and the recent Federal Reserve “pause” has supported RMB appreciation.¹⁴

Critically, the Trump administration’s efforts—to the extent they focus on currency “stability” as opposed to enhanced transparency—seemingly fly in the face of China’s efforts to develop a more modern monetary policy framework, as well as longstanding U.S., G-7, and G-20 calls for more rapid movement toward market-determined exchange rates, currency flexibility and not targeting exchange rates.

Considerations on the Use of Currency Provisions and Trade Agreements

The discussion above points to the need for an assessment of the merits of including currency provisions within the ambit of trade agreements.

Domestic political concerns are a key driver for much of the consideration. Just as Secretary Baker used the Plaza Accord to push back on protectionist forces in the mid-1980s, the Obama administration worked with Congress to develop the language on the TPA currency principal negotiating objective and the Bennet Amendment, which calls on Treasury to quantify performance using bilateral trade, current account and foreign exchange intervention. The Joint Declaration, developed with TPP partners, also reflected that reality.

While defusing and managing political tensions is to be welcomed, that does not mean that currency provisions in or alongside trade deals are a good idea.

Exchange rates are determined by a wealth of factors, many of which extend well beyond trade accounts and can swamp trade flows.

- Trade in goods and services only impact the current account. But exchange rates reflect the entirety of the balance of payments and the full range of associated underlying policies. For example, current accounts are also affected by household, corporate and governmental saving and investment decisions, which often have deeply rooted structural determinants. Fiscal and monetary policies impact interest rates, which are a critical determinant for capital flows. Investment climates and relative growth outlooks affect foreign direct investment, etc.
- It is highly unrealistic to think that the United States would alter fiscal or monetary policies to achieve given trade outcomes, let alone that doing so in the context of a trade deal would be sensible. The Federal Reserve is independent and is guided by its dual mandate. Fiscal policy is a product of messy Congressional and Executive Branch interaction that often takes little account of stabilization policy and external balance considerations.
- Trade negotiators have no responsibilities, nor expertise, in macroeconomic policy. Nor do they have a legal mandate in this regard.
- The focus on trade can be confusing. The current administration focuses on bilateral trade balances, a focus that economists dismiss. It often forgets that the United States runs a surplus on services. China has a large trade surplus, but its current account surplus is very small due to services outflows—even if one questions the accuracy of their measurement.

14. Mark Sobel, "Augmenting US Treasury Foreign Exchange Report," OMFIF, February 19, 2019, <https://www.omfif.org/analysis/commentary/2019/february/augmenting-treasury-trade-partner-report/>.

Exchange rate measurement poses enormous technical challenges.

- What exchange rate should one look at? A country's trade performance is most responsive to its effective exchange rate, weighting currency movements against all trading partners. But the current administration emphasizes bilateral exchange rates and nominal ones at that. A country's real effective exchange rate, and movements in it, is a far more important determinant of trade flows than nominal exchange rate movements.
- While reasonable judgments can be made about currency under- and overvaluation, equilibrium exchange rates and deviations from them cannot be measured with precision. There is no agreed methodology for doing so; outcomes vary depending on assumptions; and regardless, exchange rates can deviate from equilibrium levels, including for lengthy periods.¹⁵

The responsibility for exchange rate movements cannot be readily apportioned between currencies.

- The Trump administration expressed concern over RMB's weakness in 2018, warning about currency manipulation and competitive depreciation.
- But the U.S. dollar rose across the board—more against many other emerging market currencies than the RMB—as the Federal Reserve raised rates and the United States undertook a pro-cyclical fiscal expansion.
- While by definition the U.S. dollar's rise against the RMB meant the RMB fell against the U.S. dollar, the movement had more to do with U.S. macroeconomic policies leading to U.S. dollar appreciation than RMB depreciation.

Therefore, it is often far more important to focus on policy rather than currency issues.

- As discussed earlier, the imbalanced U.S. policy mix in the early 1980s had much to do with U.S. dollar appreciation, the rise of protectionism, and the Plaza Accord. Secretary Baker shot the exchange rate messenger. Despite commitments in the Plaza Accord for the United States to address its fiscal position, budget deficits remained significant over the course of the 1980s.
- Since Germany uses the euro, it does not have an exchange rate. But its persistent and massive current account surplus of 8 percent of GDP is the greatest global external distortion. The massive surplus results largely from structural and policy factors—strong household and corporate saving, including a restrictive fiscal policy, as well as low investment.
- Again, the U.S. dollar's rise versus the RMB in 2018 owed more to U.S. policy than Chinese developments.

Currency provisions raise complicated issues for bilateralism versus multilateralism.

- As the world's largest economy, the United States exerts tremendous influence and leverage over the international monetary system. It often has legitimate complaints against other countries' currency practices and reliance on U.S. demand. But U.S. currency judgments cannot be seen as neutral or impartial, even if Treasury's currency mandarins are talented and produce first-rate analysis. Again, in the 1980s, U.S. dollar appreciation would likely have been smaller had the United States pursued a less expansionary fiscal policy. The same could be said for 2018. The United States has not done a good job of keeping its house in order for significant periods, with significant spillovers to the rest of the world.

15. The IMF's External Balance Assessment in the fund's annual External Sector Report is probably the best approach, though it is still a work much in need of progress.

- The IMF was created to avoid recourse to the beggar-thy-neighbor policies of the 1930s and the bilateralization of exchange rate disputes. It is seen globally as a far more impartial and neutral actor than any single country. In some ways, U.S. bilateral use of currency provisions in association with currency agreements undermines the IMF's multilateral role. That said, while the IMF's exchange rate analysis has improved over the last decade, the IMF often steers clear of rendering crisp judgments on exchange rate valuations, currency and external issues.

What to Do in the Future?

In conclusion, U.S. perceptions about other countries pursuing harmful currency practices and unfairly relying on the U.S. economic engine is an oft-repeated story. Protectionist pressure ensued, even with full employment. The economic and technical concerns about using currency provisions in or alongside trade deals are a formidable challenge to overcome.

U.S. concerns about China's current account surpluses and reserve accumulation in the mid-2000s, plus reserve buildups after the GFC, were completely legitimate. However, U.S. macroeconomic policy—especially fiscal policy—has often been our country's worst enemy in pushing currency concerns to the fore. Undoubtedly, the intensified pressures since the Global Financial Crisis to use currency provisions reflect in part angst about technological change, globalization, and rising inequality. U.S. leaders should be far more sensitive about not throwing stones in glass houses.

Our country's leadership has failed to explain these issues to the public and instead often indulged popular sentiment. As a consequence, while the association of currency provisions with trade deals is decidedly not first-best policy, to the extent that such efforts can sensibly defuse protectionist pressures at home or worse outcomes, they can serve a useful purpose.

There are no good answers to how to deal with these conundrums. Clearly, the IMF can further step up the clarity and candidness of its exchange rate analysis, but that is a small part of the equation. Countries around the world, wishing to have no part of currency provisions in trade discussions, often for understandable reasons, should figure out how to deal with and manage relations with the United States on this front.

As noted, the United States does at times have legitimate complaints against other countries' currency practices. However, the United States must do a far better job in recognizing the inherent complexities in rendering objective exchange rate judgments and understanding the concerns of others, especially when the latter are raising legitimate complaints about U.S. policies and practices. U.S. leaders should also be far more ready and willing to acknowledge their own sins, rather than pointing fingers abroad.

In these circumstances, exchange rate issues should not be subject to dispute resolution. Nor can exchange rate discussions be divorced from broader macroeconomic and policy settings. It is far better to hold exchange rate discussions in macroeconomic channels, not trade channels. Currency provisions should be separated from trade agreements. Transparency should be essential, and thus the revised KORUS model is not likely a sustainable approach. Given these political realities, a solution akin to the TPP's "Joint Declaration," which acknowledges the importance of exchange rate and macroeconomic policies to trade outcomes but does not subject such policies to trade authorities nor to trade enforcement mechanisms, is the best of the highly imperfect options.

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