Global Conflict over Exchange Rates, Part Three

Joseph E. Gagnon and John Williamson discuss the need for greater enforcement of norms on exchange rates and reserve accumulation by the International Monetary Fund and the World Trade Organization.

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Steve Weisman: Joseph Gagnon and John Williamson of the Peterson Institute for International Economics have been discussing the problem of accumulated reserves and exchange rate manipulation by countries around the world. We've mostly been talking about Asia. This is Steve Weisman. Joe, you have found in your study that other countries that didn't go through the kind of crisis that Asia went through are also engaging in this practice. What are the countries doing that and why are they doing it? Are they just copycats for Asia or do they have their own reasons?

Joseph Gagnon: Some of both, I think. The biggest other group besides the Asians -- developing economies and newly-advanced economies -- is the large oil exporters, whose economies are so overwhelmingly dominated by oil that there isn't really a lot of room to invest at home. So they need to save some of that abroad.

Steve Weisman: Didn't the West encourage them to do that, going back to the first OPEC price hikes?

Joseph Gagnon: Yes, there was some encouragement of that. But at that point, they actually quickly turned that saving into borrowing. Saudi Arabia had a large current account deficit even when oil prices were high back in the early '80s. Now, I think they've realized that that was a mistake, but I think they've once again, as the Asian countries, have gone too far in the other direction. Yes, it would be a mistake for them to have a deficit, they should be saving. But the amount of saving is just excessive compared to their exports. They're saving half of their total oil production, which is very high. I mean, I think a number that might be reasonable might be 20 percent.

Steve Weisman: There are also a few countries in Europe, like Switzerland and Scandinavian countries, I think.

Joseph Gagnon: OK. There are some other groups. Those are the two biggest groups, Asia and oil exporters. A third group is emerging markets or developing economies that don't have large current account surpluses, but are, I think,

defensively doing some of this behavior because when other countries do it, it pushes their currencies up, too. They're trying to defend against that, and I think you might put Brazil, Mexico, and Chile in that group.

Steve Weisman: Yes.

Joseph Gagnon: And I think John and I agree, that I don't name them as currency manipulators, even though they are doing it. They have more reserves than they need for defensive purposes, but they're trying to keep their currencies from appreciating too much, because they're being adversely affected by China.

Then the third group would be Switzerland and Denmark, which have a unique situation in the whole European crisis and that's a whole other kettle of fish.

Steve Weisman: John, how do you assess the spread of this practice as a problem for the global financial system?

John Williamson: I think Joe was quite right to suggest that the Latin Americans are acting defensively. They're buying reserves, it's true, but they are trying to prevent their tradable sectors becoming completely overwhelmed by Chinese competition in particular, and I think that's legitimate.

Steve Weisman: When you say it's legitimate, do you mean that you sympathize or that they're doing what's sensible; their policies are sensible for their own needs?

John Williamson: Both things. Yes, I think I sympathize because their policies are sensible, yes.

Steve Weisman: Is this a problem? You have studied this. I think both of you think that the international mechanisms for enforcing norms are inadequate. Are there legitimate and illegitimate reasons involved?

John Williamson: Well, I agree that one needs to try and draw those distinctions, and we have an international institution which is supposed to do this and which is indeed making an effort to do it. We're going to discuss here at the Peterson Institute next month with the IMF what its new policies are for looking at exchange rates and countries' policies in regards to current account surpluses. I don't agree with all the way that the IMF has gone about it, but I'm very much in sympathy with the fact they are making an effort to insert themselves into the fray.

Steve Weisman: A final thought, Joe?

Joseph Gagnon: Yes, I agree with John. I think the IMF, the International Monetary Fund, is the obvious institution to act here. But I have proposed that the World Trade Organization could have a role, perhaps in conjunction with the IMF, because the IMF doesn't really have the ability to impose the kind of sanctions that seem most appropriate. I think the kind of sanctions against this behavior would be kind of broad tariffs that were approved in a multinational setting and the IMF really can't do that.

Steve Weisman: Thank you both.