



# FAIR CURRENCY COALITION

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## FACT OF THE WEEK

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### TREASURY'S RECORD OF REPORTS ON CURRENCY MANIPULATION

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In 1988, Congress directed the U.S. Department of the Treasury to issue semi-annual reports on exchange rates. This step was taken in light of severe misalignment of exchange rates to the detriment of the U.S. economy in the early 1980s. Congress intended that Treasury assess the impact of the U.S. dollar's exchange rate (1) on the ability of the United States to maintain more appropriate and sustainable balances in its current and merchandise trade accounts, (2) on production, employment, and non-inflationary growth in the United States, and (3) on the international competitiveness of U.S. industries and external indebtedness of the United States.

As part of this process, codified at 22 U.S.C. §§ 5304 and 5305, Congress instructed Treasury to evaluate whether any countries are manipulating their currencies to prevent balance-of-payments adjustments or to gain an arbitrary competitive advantage – the standards mandated by IMF Article IV. In the event of an affirmative finding, Treasury was directed to undertake expedited negotiations either in the IMF or bilaterally to ensure regular and prompt adjustment of the rate of exchange so as to permit an effective balance-of-payments adjustment and the elimination of any unfair advantage. Congress also authorized Treasury not to initiate negotiations that Treasury deems would have a serious detrimental impact on vital economic and security interests of the United States.

The record of Treasury's reports to date can be summarized briefly. Between October 1988 and July 1994, Treasury found manipulation by China on five occasions, by Taiwan on four occasions, and by South Korea on three occasions. During that timeframe, Treasury cited no other countries for exchange-rate manipulation. Since July 1994, no country has been considered to be manipulating its currency's rate of exchange with the U.S. dollar.

In rendering the affirmative findings during the period of 1988-1994, Treasury typically reasoned that the foreign government must be viewed as engaged in an effort to inhibit effective balance-of-payments adjustment (and occasionally also to gain an unfair competitive advantage). It based its judgment variously upon the country's (1) large

overall trade and current account surpluses, (2) large and increasing bilateral trade surplus with the United States, (3) excessive foreign exchange reserves, (4) intervention in the foreign-exchange market and other interference with the role of market forces in the determination of exchange rates, and (5) import-restrictive administrative controls over external trade. By the same token, factors such as small, declining, or negative trade and current account balances, and no intervention by the foreign government in the foreign-exchange market to dampen appreciation of its currency, were taken by Treasury as indicators of no exchange-rate manipulation.

In making its determinations of exchange-rate manipulation by China, Treasury used benchmarks substantially less striking than the current facts. As but two examples, China's foreign reserves between 1992 and 1994 were in the range of approximately \$19 billion - \$52 billion, but today are estimated at \$2.4 trillion or more, while China's annual trade surplus with the United States between 1992 and 1994 was roughly \$18 billion - \$29 billion, but in 2008 was \$266 billion and in 2009 was another \$226 billion. Noting this, it is only fair to ask why the far larger figures in recent years have not likewise led to findings of exchange-rate manipulation by China.

Moreover, even if there were an affirmative finding of currency manipulation by China, all Treasury would be obligated under U.S. law to do would be to open negotiations in the IMF or bilaterally with China in an attempt to rectify the problem – the very approach the United States has been following for roughly the last six years, including during President Obama's visit to China late last year where he raised the issue with President Hu Jintao. As is painfully apparent, China's leaders not only have rebuffed these U.S. initiatives, they have not acted upon the IMF's urgings to revalue the renminbi meaningfully. China's government clearly is wedded to an export-led model of growth without regard to the damage and severe imbalances being caused to the United States and the rest of the world.

Considering China's refusal to negotiate, it would be wise for Congress to pass the Currency Reform for Fair Trade Act, H.R. 2378 and S. 1027, the only WTO-consistent legislation that addresses the subsidy effects of currency undervaluation.

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