Protectionism and Foreign Exchange Markets

By John Beerling, Vice President, International Business Development

As the United States begins implementing protectionist policies, it may be useful to examine some of the effects that may be expected in foreign exchange (and other) markets. Keep in mind that we have recently seen strong increases in global trade overall. This situation is, however, likely to change in the face of trade protectionism.

Impact of Trade Protectionism

Currencies impacted the most negatively would be those who disproportionately trade with the U.S. and for whom trade represents a large portion of GDP. Some examples of affected currencies are CHF, EUR, and CNY. The next largest impacts would be for countries who trade significantly with China, since that is where the U.S. is directing policy. Examples of currencies influenced from this would be CAD, JPY, AUD, NZD, KRW, SGD and MXN.

Foreign Exchange Key	
Country/Currency	**Currency Abbreviation**
Australia Dollar	AUD
Canada Dollar	CAD
Switzerland Franc	CHF
Chili Peso	CLP
China Yuan/Renminbi	CNY
Euro	EUR
Hungary Forint	HUF
Japan Yen	JPY
South Korean Won	KRW
Mexico Peso	MXN
Malaysia Ringgit	MYR
New Zealand Dollar	NZD
Peru Nuevo Sol	PEN
Russian Rouble	RUB
Singapore Dollar	SGD
Turkish New Lira	TRY
USA Dollar	USD
South Africa Rand	ZAR

Commodity prices may also come under pressure as tariffs cause reduced demand for more expensive final products by U.S. consumers. Currencies such as CAD, AUD and NZD would suffer in this environment. The impact of trade protectionism would even extend to commodity exporters who do not predominantly deal with the U.S., resulting in negative effects to currencies like MYR, RUB, CLP, PEN, and ZAR.

While protectionism would likely prop up the value of the U.S. dollar, countries with a high proportion of USD denominated debt would be adversely affected. Examples of those currencies include HUF, TRY, CLP and SGD.

Local Impact

There will also be some serious local effects in the U.S. because of protectionism. Most notable is inflation. Increases in steel and aluminum costs will lead to increased prices for automobiles, aircraft, construction materials, and aluminum cans. While the U.S. may save a few hundred jobs in the steel industry, it may risk thousands more in automobile and aircraft production.

These sound like some serious effects and they are. However, all of this analysis results from only examining U.S. protectionism. As we have already heard, countries around the world will respond with their own forms of protectionism, which should put pressures on yet another set of currencies.

With so many nations battered in a trade war, the situation appears somewhat reminiscent of a global depression and trade war, not unlike the 1930's. Since that is not generally a time when we regard America as 'great,' we might assume that it is not the goal to take us back there again.

Since we have been assured that 'trade wars are good, and easy to win,' we can assume that this entire protectionist stance is merely a negotiating ploy. No serious support for that statement exists, and no plan for winning a trade war will ever be presented. China has responded to U.S. tariff announcements with tariffs of their own. However, neither side has actually enacted the tariffs. It is unlikely that they will.

Ongoing Negotiations

Both China and the U.S. admit they are currently in active trade negotiations. Both sides felt it necessary to play the tariff card to establish trade positions. Also, do not discount the political implications of the presidential announcement of tariffs on the eve of a hotly contested election in steel country. This appears to be just the opening salvo in a long round of negotiations. It does not appear either side is actually willing to risk the effects of a trade war. While winning a trade war may be 'easy,' losing one could be disastrous.

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