

# ‘It could get very serious’: Why some analysts fear a U.S.-China currency war

[Jeff Stein](#)



A man walks past a money exchange shop in Hong Kong. China's yuan fell below the politically sensitive level of seven to the U.S. dollar on Monday, adding to trade tension with Washington. (Kin Cheung/AP)

The United States and China just opened an explosive new front in their broadening economic confrontation: a currency war.

China [allowed the value of its tightly controlled currency](#) to fall to an 11-year low Monday, a move that threatens to hurt American producers by making their products more expensive for Chinese customers.

The Treasury Department retaliated late Monday afternoon by designating China a “currency manipulator,” a rare label it has only slapped on foreign countries a few times.

The twin actions were widely seen as a major escalation of the U.S.-China trade war. Analysts and economists said they fear severe economic consequences for both countries, including additional trade restrictions that could slow growth.

“It could get very serious if trade tensions between China and the U.S. morph into a currency war,” said Eswar Prasad, a professor of trade policy at Cornell University. “This could lead the U.S. to essentially shut down all imports from China.”

The latest feud kicked off last week when President Trump announced that he would impose 10 percent tariffs on an additional \$300 billion in Chinese imports, citing a breakdown in negotiations with China’s government.

China responded Monday by allowing its currency to fall to an 11-year low, crossing the threshold of seven yuan (or renminbi as the currency is also known) per dollar, a level not seen since the Great Recession. The falling value of the Chinese currency rippled through the global economy, leading to steep losses on Wall Street and rattling investors.

Trump lashed out against China over the decline, accusing Beijing of “currency manipulation.” A statement by the Treasury Department said Treasury Secretary Steven Mnuchin has “today determined that China is a currency manipulator.”

“China dropped the price of their currency to an almost a historic low. It’s called ‘currency manipulation,’ ” the president wrote on Twitter. “Are you listening Federal Reserve? This is a major violation which will greatly weaken China over time!”



Some leading congressional Democrats have backed the president in raising that concern, with Senate Minority Leader Charles E. Schumer (D-N.Y.) [calling](#) on the administration to label China a currency manipulator, according to Bloomberg News.

The fight over China's economy poses several risks, from exacerbating America's trade deficit to slowing down both nation's economies.

## **Widening America's trade deficit**

As a candidate and in the White House, Trump has made reducing America's trade deficit with China — the amount by which the United States' imports from China exceed its exports — a central priority of his administration.

But earlier this year, the United States posted a trade deficit of about \$900 billion, setting a record. America's trade deficit with China is projected to balloon over the next several years, said Robert Scott, an economic expert at the Economic Policy Institute, a left-leaning think tank. The value of the dollar has already been rising since last year.

The depreciation in China's currency means American manufacturers will have an even harder time selling their products to China and in other markets where Chinese producers compete, experts say, further widening the nation's trade deficit.

“If China continues to devalue its currency, it will continue to make the trade deficit worse — even if the tariffs reduce imports,” Scott said.

## **Severe retaliation from the United States**

The United States last named China a currency manipulator in the early 1990s and has not applied that designation since. In May, a Treasury Department report identified several red flags but stopped short of designating China a currency manipulator.

Under the designation, America could impose much more significant tariffs on China than it has so far — which could trigger further retaliation from China.

“The U.S. could use the designation as a means to impose unilateral punitive tariffs,” Prasad said. “And it would certainly also provide justification and political cover for more tariffs.”

The United States may also appeal to the World Trade Organization for a crackdown on China or successfully rally international allies to restrict trade with China.

“There’s a risk now that they view the currency depreciation as an act of economic aggression and decide to further increase the economic hostility against China,” Prasad said.

## **A drop in global demand**

But the most dangerous potential consequence of a currency battle would be a slowing of overall economic growth in the United States and China, at a time when analysts already fear a global slowdown could push the United States into a recession.

China’s growth has already slowed. A depreciation in its currency could hurt European manufacturers that compete with Chinese products, which could hurt those countries’ economies at a vulnerable time. Already, Wall Street saw its worst day of 2019, with a massive sell-off while volatility indexes soared and all 11 stock market sectors Monday were in the red.

“The financial instability associated with the trade wars will increase uncertainty and hurt confidence and investment, which can have a bigger impact on the U.S. economy,” said Mark Sobel, a former Treasury official.

The potential for higher tariffs and a devaluation of currencies has echoes of the steps that led to the Great Depression in the 1930s, said Steven Charles

Kyle, an economics professor at Cornell University.

“We don’t want to be even on the first step of this path. This is EXACTLY what happened as the Great Depression really got going in the 1930s: Everyone erected high tariff barriers and tried to out-compete their trading partners in devaluing (depreciating) their currencies,” Kyle wrote in an email. “A few years of that and world trade ground to a near total halt.”