“Exchange Rate Responses of Emerging Markets to Expected Protectionist U.S. Trade Policies”

Discussion

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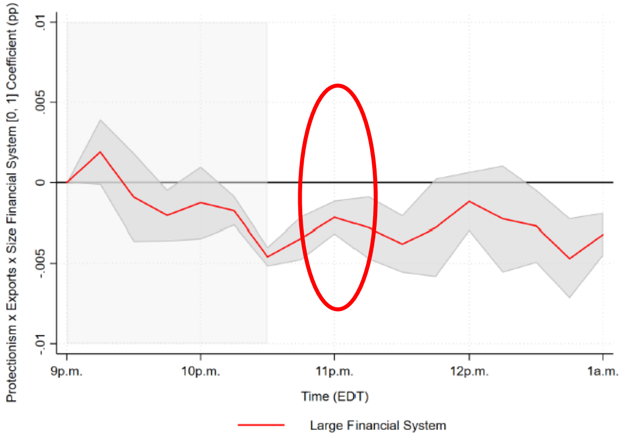
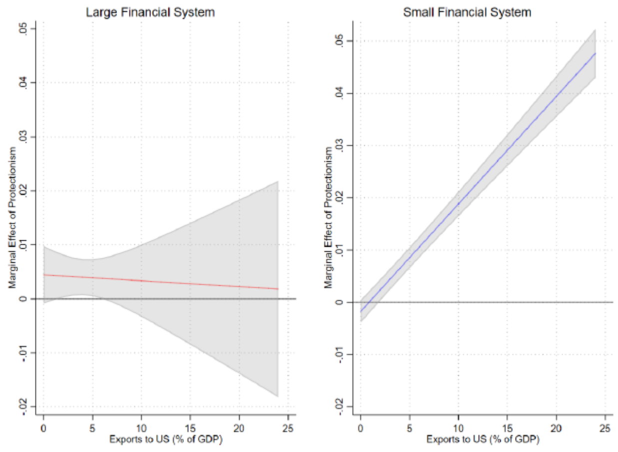
Short summary of the results

- How the US presidential TV debates outcome, focusing on the election probabilities of the protectionist candidate, impact emerging market (EME) exchange rates
  - Significant unconditional debate effect indicating US dollar depreciation
  - Immediate foreign currency depreciation as the protectionist candidate's probability rises
  - This impact is stronger with higher exports to the UD
- How macroeconomic characteristics affect the results
  - High levels of **FX reserves** may dampen the depreciation pressure
  - **Restrictions on capital movement** may mitigate exchange rate vulnerabilities
  - Countries with **smaller financial markets** are less resilient
  - Stronger **financial linkages** with the US via equity exposure enhance the exposure towards trade policy uncertainty
  - Greater **trade integration** with the US amplifies exchange rate vulnerabilities
  - **Stronger political institutions** can mitigate exchange rate vulnerability

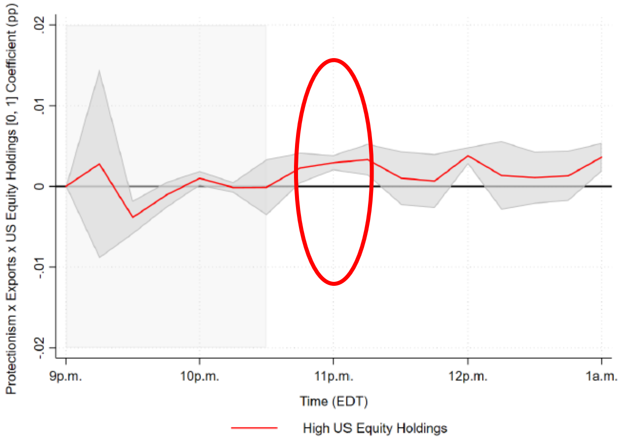
How to read the results?

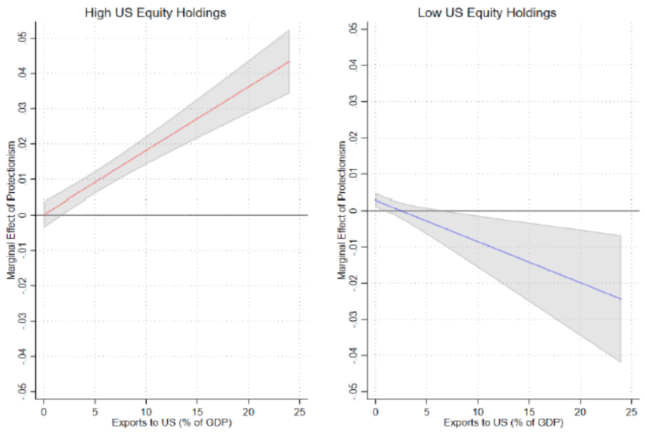
- TV debates between 9:00 and 10:30 EDT, sometimes the results are obvious





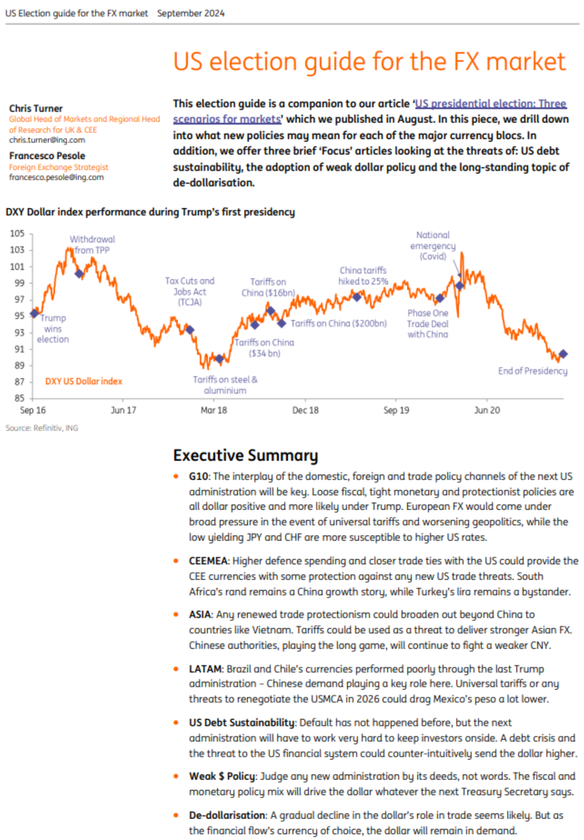
- Sometimes the results may change every 15 minutes





How to read the results?

- How long-lasting are the effects of the TV debate on exchange rate?
- Is the outcome of the debate reflecting to some extent the election results? Potentially yes ([Shaw & Roberts, 2000](#))
- Can we say something about the exchange rate movements after the election (e.g., [Wolfers & Zitzewitz, 2016](#) shows how the Trump victory would reduce the value of S&P 500 and the oil price)?
- Is the outcome an "unexpected" exogenous shock, or one of the potential scenarios?
- Is there any space for "speculative investments", or alternative drivers of the results?



US Election guide for the FX market September 2024

US election guide for the FX market

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This election guide is a companion to our article '[US presidential election: Three scenarios for markets](#)' which we published in August. In this piece, we drill down into what new policies may mean for each of the major currency blocs. In addition, we offer three brief 'Focus' articles looking at the threats of: US debt sustainability, the adoption of weak dollar policy and the long-standing topic of de-dollarisation.

DXY Dollar index performance during Trump's first presidency

Source: Refinitiv, ING

Executive Summary

- **G10**: The interplay of the domestic, foreign and trade policy channels of the next US administration will be key. Loose fiscal, tight monetary and protectionist policies are all dollar positive and more likely under Trump. European FX would come under broad pressure in the event of universal tariffs and worsening geopolitics, while the low yielding JPY and CHF are more susceptible to higher US rates.
- **CEEMEA**: Higher defence spending and closer trade ties with the US could provide the CEE currencies with some protection against any new US trade threats. South Africa's rand remains a China growth story, while Turkey's lira remains a bystander.
- **ASIA**: Any renewed trade protectionism could broaden out beyond China to countries like Vietnam. Tariffs could be used as a threat to deliver stronger Asian FX. Chinese authorities, playing the long game, will continue to fight a weaker CNY.
- **LATAM**: Brazil and Chile's currencies performed poorly through the last Trump administration – Chinese demand playing a key role here. Universal tariffs or any threats to renegotiate the USMCA in 2026 could drag Mexico's peso a lot lower.
- **US Debt Sustainability**: Default has not happened before, but the next administration will have to work very hard to keep investors onside. A debt crisis and the threat to the US financial system could counter-intuitively send the dollar higher.
- **Weak $ Policy**: Judge any new administration by its deeds, not words. The fiscal and monetary policy mix will drive the dollar whatever the next Treasury Secretary says.
- **De-dollarisation**: A gradual decline in the dollar's role in trade seems likely. But as the financial flow's currency of choice, the dollar will remain in demand.

Other questions

- Econometric specification: up to 5 466 trading days, 23 debate days, i.e. only 0.42% of all observations
    - some discussion may be needed as some variables have an excess number of zeros (Eisenberg et al, 2015)
- How to deal with countries where the FX regime changed
    - e.g. Slovenia joined the Eurozone in January 2007, Slovakia in 2009, Estonia in 2011
- Have authors thought about some combined impact (not only 1 macroeconomic factor at once + exports to the US)
    - E.g. FX reserves + capital account openness or financial market size?

Thank you for your attention!