ANALYSIS | Falling loonie part of a new race to the bottom

A new outbreak of beggar-thy-neighbour threatens global growth and stability

By Don Pittis, CBC News Posted: Jan 29, 2015 5:00 AM ET | Last Updated: Jan 29, 2015 9:47 AM ET

Oil-exporting countries like Russia are watching their currencies fall with petroleum prices. But as others push interest rates down and print money, their currencies are falling, too. (Dmitry Lovetsky/AP)

In the Cold War it was called nuclear escalation.

Each time one side upped its missile count, the other would up it more. Soon both sides were so bristling with missiles that the only possible strategy was mutually assured destruction, or MAD, which threatened to send much of Europe and North America back to the Stone Age.

Fortunately, a currency war does not have the same destructive capacity. But the principle of escalation is the same. And just as in the nuclear example, despite repeated talks to get it under control, new outbreaks of escalation keep happening.

- **Loonie drops below 80 cents US**
- **Canadian dollar could fall to 75 cents**

In a currency war each round of escalation is the process of making your currency worth less. And in this war, Canada is a full participant.

As economists repeatedly tell us, the falling loonie is bad for Canadians who want to travel abroad. It also makes life more expensive for people who want to buy foreign goods, from European cars to South Korean washing machines.

Boost to exports

But on the bright side, they tell us, it will be good for the Canadian economy.

Our products will become cheaper in foreign markets, boosting our industrial economy as we export more to the thriving U.S. economy.

And while working to encourage Canadians to holiday at home and shop

About The Author

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Don Pittis has been a Fuller Brush man, a forest fire fighter and an

AMANDA LANG

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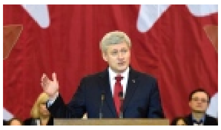

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Arctic ranger before discovering journalism. He was principal business reporter for Radio Television Hong Kong before the handover to China and has produced and reported for CBC and BBC News. He is currently senior producer at CBC's business unit.

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at home, it will make people with higher currencies want to shop and travel in Canada.

- **Weak loonie will sway snowbirds, cross-border shopping**

Central banks around the world, including China, have been cutting interest rates, pushing down the value of their currencies. (Associated Press)

Of course that only works if everyone else's currency stays high. And in currency wars that's not what happens.

The ruble is down by half. The euro has hit 11-year lows after countries using it began printing money. Japan has been printing money, too. Denmark has cut interest rates to keep the krone from surging against the falling euro.

India and China have cut. Yesterday, **Singapore joined the pack**, saying it was worried about deflation.

We've seen it all before. I first noted it in 2009 when world leaders and bankers were all trying to talk down the value of their money. About a year later Brazil's finance minister officially complained, coining the term currency war. After each new complaint, countries meet to try to hammer out friendly agreements to keep their currencies in balance.

- **The race for the world's crummiest currency**
- **World economies rearm for a trade war nobody wants**

One of the reasons thoughtful economists don't like currency wars is that manipulating your currency is a well accepted barrier to trade of the kind that seized up global commerce in the 1930s. Pushing your currency down has a similar effect to putting a restrictive tariff on imports.

This means war

Since the Brazilian minister coined it, the term currency war has been adopted by an odd conspiracy theory that warns of inflation and a run on gold. But instead, as U.S. Fed Chair Janet Yellen said yesterday, she is more worried about deflation as the prices of U.S. imports fall.

This is only one example of how economic contagions spread across international borders. There are others. U.S. corporate results have not been as good as expected because when companies bring their profits home they are worth less in dollars. Companies are also worried about future sales as U.S. goods become more expensive. U.S. car makers will face stiffer competition from Japanese and European imports.

Much of the world, including Canada, has been counting on a strong U.S. recovery. But the United States can't buy everyone's exports if theirs collapse.

Oil effect

It is reasonable that currencies of countries like Canada and Russia that depend on oil exports will fall with the price of petroleum. That's the way currencies are supposed to work. But Canada has gone beyond that, cutting rates once and hinting it will cut again.

No central bank says it is cutting interest rates or printing money as a trade barrier. There is always another good reason. But the result may be that when everyone pushes their currency down it will force places with strong currencies to put up subtle trade barriers of their own.

And rather than helping the world economy, that would be a matter of mutually assured destruction.

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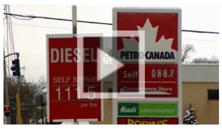

Canada's shrinking GDP

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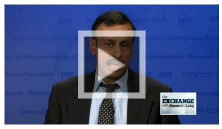
Canada's gross domestic product contracted by 0.2 per cent in November, as the economy was dragged down by lower oil prices and unexpected weakness in manufacturing and mining



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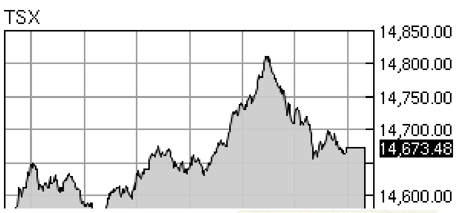

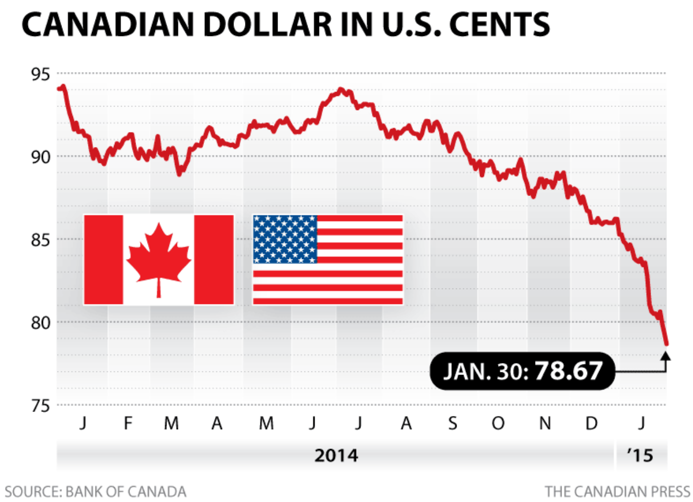

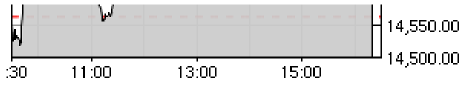

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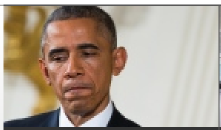

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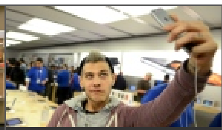

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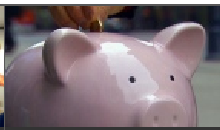

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