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THE VIEW
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The art of trade war

With accusations of economic warfare being levelled at various countries, it should be remembered that such measures ultimately benefit no one

Remembrance Day at the Cenotaph in Central is a remarkable display of respect for those who fell in the first world war or who have lost their lives serving others in the disciplined services, such as the police and fire brigade.

They are remembered in a ceremony representing six different religions in five languages in a striking outpouring of accord that makes Hong Kong proud. On their ultimate sacrifice we have built our lives.

The analogy of war is often used in economics. The Chinese military strategist Sun Tzu said "the supreme art of war is to subdue the enemy without fighting". Could he have been describing economic warfare?

Warfare implies a ruthless act of harm to the other side. For instance, the Germans printed millions of forged British banknotes to try to destabilise the British economy in the second world war.

It only failed because the notes could not be physically delivered in sufficient quantities.

However, when the market talks of economic warfare, it is

usually less of a conspiracy and more a comedy of errors. We charge the Japanese of waging currency warfare, to beggar thy neighbours by making Japan's exports cheaper, just because the yen has collapsed 15 per cent since August.

Such wild talk ignores the fact that most major currencies such as the euro and sterling have also weakened in that time.

The yen has weakened more because the inflexible Japanese economy has been so poorly managed for 25 years. It would have collapsed long ago but for a false aura of invincibility to a dim-witted foreign exchange market. It also forgets that much Japanese-owned industry is now in the United States, Europe and China, removing the simple export benefit.

Such things are not war, but are the naturally occurring process of economic rebalancing.

Few countries succeed in using their currencies as a weapon without damaging another feature of their economy. Russia has spent billions of hard currency dollars this year defending the rouble, only to see it fall 31 per cent.

Mainland China's closed-to-



Few nations use currencies as a weapon without damaging their own economy

foreigners equity, bond and currency markets have hindered the development of the healthy capital markets needed at this stage of development.

We hear that nations are using the oil price, now at 4-year lows, to wage war against each other. Falling crude was blamed on the Americans trying to push the price down to hurt the Russians, or perhaps the

Russians trying to stymie US investment in the more expensive shale oil.

More recently the biggest oil exporter, Saudi Arabia, was blamed for pushing prices down, only for the data to show that it had actually been trying to support the price.

Trade wars, discussed in Beijing at the recent Asia-Pacific Economic Cooperation meeting, and in Brisbane at the G20 last week, are often suspected but rarely proven.

Protectionism, currency manipulation, government subsidies, health and safety, are all used as excuses by countries to adjust the terms of trade in their favour but they are pretty blunt weapons of war, because at the end of the day, Sun Tzu was right – economics wins.

Firing economic weapons at somebody else usually blows up in your own face.

Economic tools like oil subsidies, money printing, or price controls in countries like Argentina, India, Venezuela and Zimbabwe, have driven products off the shelves, sent prices through the roof, and brought countries at times to near-bankruptcy.

Markets may produce outcomes that we do not like, but the best remedy is to gently rebalance the playing field from time to time. Unfortunately,

politicians find action requires time that they do not have.

Naturally countries will try to nudge, intervene and manipulate currencies, interest rates or prices to their own advantage.

It usually does not work for long. As Bill Clinton said, "it's the economy, stupid" – and supply and demand, price and volume, credit and debit will eventually correct manmade imbalances. There are very few economic war initiatives – only good economic management.

Hong Kong is firmly in the crossfire of this tweaking and manipulation by major countries but we can do little to protect ourselves.

We have an economy rooted in the mainland, yet with our two vital economic tools, our currency value and interest rates, determined by the US and global economies.

Sometimes it will be a perfect confluence, at other times a perfect storm. The recent volatility in markets is a foretaste of how flexible to change we have to be.

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