Currency Fluctuations Cause Consternation for Importers

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Dramatic fluctuations between the dollar and the currencies of key apparel and textile sourcing countries, including China, India, Pakistan, Bangladesh and Turkey, has put U.S. importers in a difficult position.

Experts put much of the blame on the “soft” dollar that has evolved in the last few months as Federal Reserve policy shifted to propping up the currency and holding down interest rates to letting it float more freely and starting a period of gradual rate increases.

China’s slowing economy has also played a role in the currency fluctuations, as has the strengthening of many developing economies.

Chinese yuan vs. U.S. dollar: Source; XE

Guido Schlossmann, president and chief executive officer of Synergies Worldwide Sourcing Co., said it comes just as the Lunar New Year will shut down production in China and Vietnam, and as retailers and brands need to place order for the fall and winter season.

Importer's impasse

The Chinese yuan has depreciated 10 percent in the last year, Schlossmann said, "which will have an impact on China and the surrounding sourcing countries." The Chinese yuan was trading 6.20 to the dollar on Monday compared to a recent peak of 6.92 in March.

"A lot of American importers still favor China due to flexibility in minimum order quantities and lead times, and they have been very hesitant to go to Bangladesh and Pakistan," Schlossmann said. "Some think the Chinese government will try to ease the pain by giving indirect or direct subsidies," even though this may not be completely above board.

"The result could lead to erosion of margins and profitability, especially for traditional U.S. retailers," he added.

[Read more about U.S. imports: US Denim Imports Continue to Shift in Favor of Low Cost Countries]

Bangladesh taka vs. U.S. dollar: Source; XE

Pakistan rupee vs. U.S. dollar: Source; XE

Meanwhile, Bangladesh saw a steep depreciation of the taka against the dollar from April to December, then it bounced back, but it's still down about 5 percent on a year-to-year basis. The taka was trading at 82.92 to the dollar on Monday compared to peak of 84.95 in November, rebounding from 79.5 a year ago.

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"It gives Bangladesh an additional cost advantage and makes it more competitive," Schlossmann said.

The Indian rupee in 2017 appreciated about 8.92% and combined with a reduction in direct export subsidies, had led to a cost increase of nearly 10 percent. The rupee was trading at 64.16 to the dollar on Monday compared to peaks of around 65.5 in November and 67.35 a year ago.

Indian rupee vs. U.S. dollar: Source; XE

The Pakistan rupee has been stable, though in December it crashed and recovered a bit, but year-on-year it’s still down 4.6%, which similar to Bangladesh, makes the country more competitive. It has gone through wild swings with highs of late reaching to roughly 110 to the dollar from 104.5 a year ago.

“These aren’t necessarily big percentages, but in our still very price-sensitive world, that means something,” Schlossmann added.

Also in the mix for importers is Turkey, which has seen its lira bounce up and down against the dollar. It now trades at 3.77 to the dollar, with swings as low as 3.41 and as high as 3.96 in the last six months.

Turkish lira vs. U.S. dollar: Source; XE

“I believe if there is no interference by the Chinese government, certain product categories may migrate somewhere else,” said Schlossmann, citing Myanmar and Vietnam as possibilities for outerwear sourcing, for example.

Denim production could shift out of China to Pakistan, Bangladesh and Turkey, where there are already established factory infrastructures.

The dollar dilemma

Joel Prakken, vice president, chief U.S. economist and co-head of U.S. economics for Economics and Country Risk at IHS Markit, explained that what’s behind the so-called “soft dollar” that’s causing some of the currency fluctuations is cyclical.

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The U.S. went through a round of “monetary easing,” that made the dollar perhaps unusually strong, which caused other currencies to follow suit to catch up.

“What’s happened now is that our monetary tightening is under way and fully wrapped into currency evaluations,” Prakken said. “And now in some of the major countries overseas where growth has started to perk up, these countries are now moving toward their monetary tightening cycles, and in that sense will be catching up to the U.S.”

As the dollar strengthens, U.S. goods and service become less competitive in global markets, he noted, losing export share—and the trade deficit worsens. Now that process is reversing, and as the dollar comes down, exports grow and imports become more costly.

When the dollar strengthens against the currencies of the import countries, it makes their goods and services more competitive, and the opposite is true when their currency moves in the other direction.

Prakken said most economic forecasters will say the dollar is the hardest to predict of all such vehicles, however, he explained, “Our sense is that the dollar will be range bound close to its current values in the next several years. There’s a balance of upward and downward forces we’re thinking about. Interest rates are higher than the rest of the world and that supports the dollar, and there are benefits of the recently passed tax act that would seem on paper to be dollar positive. Downward forces are that as global economies perk up, their monetary cycles will start catching up to ours, and the U.S. current account deficit is fairly large, and that puts some pressure on the dollar, as well. So for the next couple of years, I see these two forces fighting themselves to a standoff.”

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An International Monetary Fund study, “Global Trade and the Dollar,” emphasized that “the U.S. dollar exchange rate drives global trade prices and volumes” because it “plays an outsize role in driving international trade prices and quantities.”

The strength of the U.S. dollar is a key predictor of rest-of-world aggregate trade volume and consumer and producer price inflation, the IMF said.

“Exchange rate fluctuations impact a country’s trade competitiveness, inflation and output, and therefore have important consequences for its welfare and economic policy,” according to the study. “It is common practice to estimate this impact by examining the pass-through of bilateral or trade-weighted exchange rates into export and import prices and volumes.”

The way out

Deepika Rana, president of strategic initiatives at Li & Fung with responsibility for the Indian Subcontinent, said currency is just one factor for importers and exporters when costing garments or fabrics.

“The way we do it is we look at all the factors that go into production together,” Rana said. “We look at fabric, currency, wage and energy efficiency, and we kind of do an equation, and then we get the net impact of the changes by country.”

Rana said currency fluctuations can account for up to 50 percent of the cost of goods sold, the largest factor followed by wages, fabric and energy. She noted that for countries with a low wage rate, like Bangladesh, currency has a higher impact on cost.

Currency fluctuations also have a greater impact for countries that aren’t as vertical, since they have to import raw materials before they manufacture the finished goods and export them, feeling the effects on both ends of the supply chain.