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EFFECTS OF CURRENCY DEVALUATION UPON DEVELOPING NATIONS: GLOBAL EFFECTS OF YUAN DEVALUATION

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Abstract

The motivation to conduct this assessment was to gauge devaluation, its cause, and consequences on the developing economies, shedding light on the recent devaluation policies of China to lower its exchange rate. Based on the theoretical analysis, devaluation of currency has an important implication in developing nations resulting in improving trade balances if the country is in a state of distress. However, this is only possible when the elasticities of export and import demands for commodities result in a value greater than one. An empirical review of the literature suggests the little impact of devaluation on the Asian developing economies when considered in large samples; reason following could be from a high dependence on imported items to the slow response to cater the demand for exports in the markets for manufactured goods and primary commodities. However, as the sample size is reduced to developing countries with the relatively greater level of industrialization and stability, the impact of devaluation on improved trade balances was visible and led to economic development. The basic motivation of this research paper is to assess the Chinese Yuan's devaluation on the Asian economic region of trade presented in the following case study.

Keywords: Devaluation, Economic Development, Developing Economies, Chinese Yuan

INTRODUCTION

(Kalyoncu et. al., 2008) emphasize the relationship of real exchange rate and economic growth, in terms of the level of output, to be an emerging issue in economics and business. The devaluation of a country's currency is looked upon as a key tool towards economic development for the improvement of international trade.

Exchange rate policy in developing countries, specifically devaluation, has long been used to improve a country's trade balance. Policy makers expect the switching of economic expenditures towards the production of more tradable goods leading to higher exports by the implementation of nominal devaluation in the currency. However, this also burdens the government with higher import bills. Thus, it is important for policy makers to critically evaluate the effects of exchange rate manipulation on imports and exports of the country, and ultimately its Gross Domestic Product (GDP), (Mujahid and Zeb, 2014).

In Pakistan, for example, the exchange rate policy throughout the 1950s remained an attractive decision. The country noticed its first trade surplus during the 'Ayubian Era' of 1959's devaluation of the Pakistani Rupee. During Bhutto's government in 1972, the Rupee was again devalued for the second and last time, which led to a favorable and positive trade surplus. Following, several trade policies were practiced in Pakistan, but they could not bring about the positive result of trade surpluses. Until the 1970s, controversies did not exist about devaluation's effect on economic growth. It was approved throughout that a devaluation policy would improve the trade balance, boost employment and output, and reduce Balance of Payments (BOP) deficits (Mujahid and Zeb, 2014). The progressive effect of devaluation results in the domestic country's imports becoming relatively expensive to its exports. Hence, local demand for goods shifts towards domestically produced capital goods and consumption goods, thereby boosting the exporting industries of the country in the international markets as well as the entire domestic economy.

Planned devaluation, cited in most textbooks explaining the orthodox theory of international trade, may not always be a necessary step towards economic growth prospects. It may, in fact, turn out to be disruptive as it hinders with the free market forces, (Reinhart, 1994). The theory states that a relatively open market system will automatically adjust to the trade deficit by a reduction in the country's price levels (through the outflow of money which will lead to a decline in prices, thus depreciating the real exchange rate). Theory concludes that this will lead to the country's goods becoming more competitive, thereby expanding exports and moving towards a favorable trade balance. However, a controversy remains whether this theory actually implies in reality. Still debated, the theory is supported by the J-curve effect that in the long-run, a devaluation does have a positive impact on trade balances. The J-curve effect will lead to a trade deficit in the short-term, leading to lower output and unemployment, before improving, as shown by the figure below. An explanation of this effect could be the immediate fall in prices not followed by an immediate fall in unit demand for goods, thus leading to an immediate fall in export revenues initially.

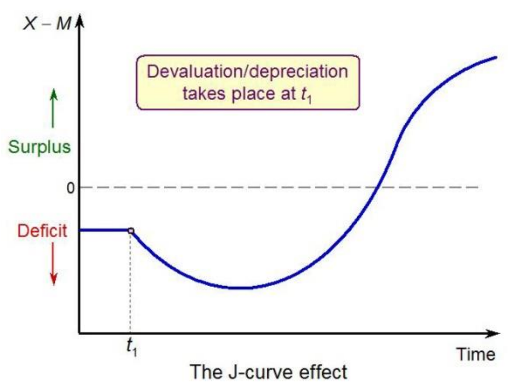

Figure 1: J-Curve Effect of Devaluation

Developing nations are often confronted with the decision of whether to devalue their currency or opt for internal or external debt financing to reduce large trade deficits. The hypothetical Marshall-Lerner condition states this phenomenon claiming that in order to increase exports, leading to a favorable trade balance, the price elasticities of demand for exported and imported goods needs to be greater than unity, (Musila and Newark, 2003).

Developing countries with trade deficits and balance of payments difficulties are usually faced with currency devaluations, (Cooper, 1971). These changes in currency affect economic growth (expansionary and contractionary). Development organizations like the IMF favor their member developing countries for devaluation to make the country's goods more competitive in the international markets and to prosper domestic firms besides the financial aid and loans that that they offer. Although this improves domestic output and international competitiveness of exports, (Krugman & Taylor, 1978) examined the adverse effects of devaluing the currency. With an initial trade deficit, devaluation would result negatively on aggregate demand, concluding, that the larger the initial deficit, the greater the contractionary effect of devaluation.

This paper recapitulates the effects of currency devaluation in developing countries on economic growth. Secondly, a basic foundation to understand the theory behind this change has been framed under the conceptual framework. Following this, an empirical review of existing theoretical studies carried out on the impacts of devaluation on developing country's GDP has been outlined. The paper includes the necessary case study on China's recent Yuan devaluation and how it affected developing importing nations. The study is completed with a couple of remarks and proposals for future exploration.

CONCEPTUAL FRAMEWORK

DEVALUATION

Devaluation' refers to the conscious lowering of a country's exchange rate. Whether the country is practicing a fixed or floating exchange rate regime, devaluation occurs due to deliberate policy initiatives by the government or the central bank to alter the exchange rate. Devaluation lowers the purchasing power of the holder of currency. In other words, the currency buys less of the other currency. Stated another way, each bill of currency buys fewer bills of another currency than before. Devaluations are most often witnessed in developing countries.

Distinguishing between Devaluation and Depreciation

The words devaluation and depreciation are often confused in everyday usage. However, the distinction between the two exists. Devaluation occurs only in those countries who are members of some fixed exchange rate system. Devaluation is usually the result of government or central bank's monetary policies. Depreciation of a currency is a fall in the external value of the currency against another due to the result of the demand and supply-side factors prevailing in the market.

In a country running a fixed exchange rate system, devaluation of currency takes place. However in a floating exchange rate system, depreciation of a currency takes place. However, excessive selling of a country's currency by the government may cause depreciation to occur.

DEVELOPING NATIONS

To understand the meaning of developing nations, it is important to address the definition of a developed nation. A country with a relatively high economic growth level and security is defined as developed country.[1] Countries are evaluated as being developed, developing or under-developed under certain established criteria. These are Gross Domestic Product (GDP), Gross National Product (GNP), the level of infrastructure, the rate of industrialization, a general standard of living, including non-economic factors such as the Human Development Index (HDI). The HDI measures the relative rate of literacy, education, and health of a country.

Developing countries in some literature may also be referred to as emerging economies and third-world countries. The World Bank classifies developing countries based on their gross national income (GNI) per capita, or as Gross National Product (GNP).[2] The World Bank states that developing countries reflect lower social and income indicators. For example, they have lower per capita income and range among low to middle-income nations, as per World Bank's rankings of countries based on income.

According to the United Nations, words such as third-world countries, developing or emerging countries are used to refer to those countries who are unable to enjoy the same level of industrialization, economic activity, and growth as developed nations. The UN Conference on Trade and Development (UNCTAD) signifies that developing nations are faced with greater development difficulties, mostly due to their geographic locations and surroundings, and are thus more prone to the risk of being unable to drive their economies out of poverty. Such countries reflect low standard of living, relatively underdeveloped industrial base and a moderate level of literacy and HDI (Human Development Index). The HDI measures a country's literacy, poverty, education and life expectancy relative to other countries around the globe.

FACTORS (REASONS) LEADING TO CURRENCY DEVALUATION

Expand Exports Demand

The initiative to devalue a currency usually comes about when it is realized that a country's currency is overvalued relative to other countries' currencies. This initiative may also be used as a policy instrument to pull out of an unfavorable balance of trade or to take benefit of short-term export revenues. Policies to devalue are usually aimed at boosting exports of the country, however, such initiatives do have counter-effects, and thus making this planned devaluation a risky policy tool. Furthermore, a devaluation policy steps taken by any country may be followed by other countries also doing the same, thereby, undermining the strategy taken by the initial country.

Devaluing favors exporters by making their goods more valuable and competitive in the global marketplace. A government seeking to devalue its currency is, in fact, trying to discourage the nation to import in bulk quantities and pressuring the current account's balance of trade. Although, this helps to counter BOT (Balance of Trade) problems, it must be noted however that, local industries, who are majorly dependent on imports for the production processes are badly hit by this initiative. They are thus forced to look for locally produced raw materials and services. This, in turn, positively, boosts local aggregate demand in the country, increases money circulation and boosts employment locally.

Trade Deficit Reduction

In another perspective, developing countries are often subject to currency hitches for which they need to implement a devaluation strategy. This may be during large trade deficits, low aggregate demand for products produced locally, or budget deficits. According to the economic theory, consistent trade deficits in the economy may lead the country into serious debt burdens and economic slowdown. In order to reduce trade deficits, devaluing a currency makes exports cheaper compared to the country's imports. This leads the balance of payments to improve as the policy prevails. One major factor, for example, that prompted the financial crises in Asia during the 1990s was due to the excessive selling of Asian

[1] Developed Economy Definition | Investopedia http://www.investopedia.com/terms/d/developed-economy.asp#ixzz3r6V66EI5

[2] The World Bank. FAQs: About Development

currencies leading to the sharp decline (depreciation) in their intrinsic values.

There are counter-effects, however, for any policy stand. The devaluing of currency will make a country's debt servicing more expensive for loans that are denominated in foreign currencies. The lower value of the currency will make it difficult for the country to pay back loans; larger amounts would now be required to pay the same loan before the devaluation, leading to decreased public confidence in the local/domestic currency.

Exchange Rate Policies

On the technical perspective, countries are subject to devaluations due to the prevalence of exchange rate controls policies. In the absence of such policies, devaluations would still occur, but it will never be a planned effort to drive the value of the currency down. Nevertheless, all countries practice some degree of currency control policies for the stability of their economy. These may be in the form of open market operations of through aggressive price controls. Developing countries are the ones which are subject to such policy measure due to their ambiguous economic prospects.

ADVANTAGES AND DISADVANTAGES OF CURRENCY DEVALUATIONS

Advantages of Devaluation[3]

Stated below are the advantages to a country for devaluing its currency:

- Cheaper and more competitive exports, which boost local demand for goods and services, leading to the creation of local employment in the export industry.
- Increased exports result in an improved balance of trade and current account balance, especially if the country was facing difficulties in marketing its products in foreign markets due to poor price competitiveness.
- Large government debt servicing at fixed rates will become cheaper over the long run as the value of currency decreases.
- Increased exports will result in long-term economic progress for the country.

Disadvantages of Devaluation

Some of the disadvantages or adverse long-term effects of devaluation are as follows:

- May lead to inflation in the long-run. Expensive imports will be reflected in higher prices for the goods produced by the firms whose raw materials make up a major proportion of imports.
- Exporting firms will have less incentive to innovate and produce efficiently, and will become dependent on the devaluation strategies to improve competitiveness.
- Reduces purchasing power of individuals who are willing to pursue vacations abroad.
- Foreign investors feel insecure holding debt securities issued by the government of the devaluing country as it will be reducing the value of their holdings.
- Individuals' cost of servicing the debt of foreign loans, mortgages, etc. will face a rise in the amount of interest costs that will be needed to repay the debt.

Keeping in mind the above advantages and disadvantages of currency devaluations, the impact of this policy measure depends on the following three factors:

1. **Business Cycle Stage**
   If a country is in a state of recession, a devaluation initiative is less likely to lead to higher inflation rates in the economy. However, if an economy is in it boom stage, such a policy measure is likely to cause increased consumer prices in the economy.
2. **Demand Elasticity**
   If demand for exports of the country is price inelastic, a devaluation will take some time to reflect improvements in the current account balance. The greater the price elasticity of demand, the quicker the impact of devaluation will be reflected in terms of the balance of trade improvements.
3. **Exchange Rate System**
   If a country has lost its competitiveness in the international markets due to it practicing a fixed exchange rate system, a devaluation may help in resolving this poor competitiveness in foreign markets.

[3] **Tejvan Pettinger** (2013), http://www.economicshelp.org/blog/1299/economics/advantages-and-disadvantages-of-devaluation/

IMPACT OF DEVALUATION

Exchange rate devaluation which nations frequently use to overcome financial crisis could bring about the unfavorable impact on nation's economy said by International Monetary Fund (IMF). In its World Economic Outlook published in Lima, Peru it said, "Conversion scale deterioration has by and large been a helpful cushion for nations encountering development obstruction – and has as of now been significant – however, could bring about antagonistic monetary record impacts if there is an involvement of foreign exchange.

In his introduction at the World Economic Outlook Press Conference, Mr. Maurice Obstfeld said, "No single arrangement of policies is appropriate for each nation trying to enhance development execution or raise flexibility. In any case, some well-known general standards still apply. Countries and economies which are under development should be prepared for monetary policy standardization by the United States. Propelled economies must keep on managing emergency legacies they persevere. In the meantime, monetary adjustments ought to proceed with where productivity gaps are negative, supplemented by monetary measures where financial space grants. Specifically, the case for infrastructure speculation appears to be convincing at a span of low long-term actual interest rate.

"Output growth has substantially increased by higher investment, yet it is positively influenced by targeted structural reforms. Such changes help to upgrade future development, as well as to expand the versatility of development. In all nations, maintained empowerment of micro- and macro-prudential strategies will likewise provide flexibility to financial crisis, whether arising locally or from abroad" Considering the problems standing up to the worldwide economy Obstfeld said "firstly, China's monetary change – far from exports and investment drove development and mass-production, providing higher attention on expenditure and utility. This procedure, however, fundamental and sound in the more extended term, has close term suggestions for China's development and its relations with its exchange collaborator."

"Secondly, the declining production costs. A long time of high worldwide interest drove costs increased and stimulated investment in production segments. yet, as China started to moderate earlier all along the present decade, numerous production costs rotated toward the ground, beginning in the latter half of 2011, and their fall has quickened in recent past.

"Thirdly, there is the approaching standardization of financial strategies in the United States. Moderately positive feedback and cost execution in the U.S. could soon legitimize a financing cost increment, yet the conceivable worldwide repossessions, particularly in rising and creating economies, increase present instabilities".

He said, "In the midst of these advancements, we anticipate that in the close term comprehensive development will continue to be cautious and changeable, with larger perceived risks. The "blessed chalice" of vigorous and synchronized worldwide extension stays tricky.

Last July IMF made a forecast that real GDP increased by 3.4% globally in the previous year but this year it will grow by 3.1 per cent only. Yet, there is a silver coating. For 2016, we anticipate a bounce back to 3.6% increase.

"As usual, the total figures cover assorted prospects crosswise over nations. Significant war makers, prominently Canada additionally Australia and Norway, are encountering log jams. Alongside the fall in genuine salaries because of poor terms of exchange, there are additionally negative venture impacts in the goods making divisions, which have demonstrated a huge headwind to development even in the United States. Yet, the decline in product costs, which, as noted, has quickened currently, is having its most emotional impacts in the rising and creating merchandise exporters. For this set of nations – which now reflects too well over a portion of world GDP will even now create the lion's offer of world development – 2015 development is anticipated to tumble to 4.0 percent from its 2014 level of 4.6 percent. This rate of development is much lower than what IMF found in the worldwide recession, and reflects the fifth straight year of falling GDP increase for rising economies.

"While products are a major a portion of the story, they are not the entire story: now and again, political unsteadiness could be a greater variable or a shade of obligation after capital inflows and over-investment prior this decade."

"With expanded conversion scale adaptability, higher international trade savings, expanded dependence on FDI streams and local currency independent financing, and usually more stable conceptual framework, numerous developing markets have expanded their strength to outside stuns."

In a few economies, the prospect of downfall remains. There is additionally the danger of a quick decomposition of security prospects premiums, prompting an increase in longer-term loan costs. Undoubtedly, we have as of now seen some of this for some rising and creating economies, specifically goods exporters.

METHODOLOGY OF THE STUDY

This review study has used existing literature on the effects of currency devaluation and how its impacts developing nations to discuss and conclude how the devaluation of a country's currency can impact a developing nation's economic growth and international business activities. This discussion was conducted a general search of papers available online on various databases like Google, MRPA, Endeavour, and Springer Link, named as Currency Devaluation's Effects on Developing Nations. A number of cited works were found on this topic and empirical study of the literature was conducted over the most relevant papers that related closely to the theory and practice of devaluation's effects on developing nation's growth. The empirical review has been summarized based on the author's objectives, findings, and methodologies used and their conclusions based on the present effects of devaluing the currency and how a developing country's trade balances, economic growth and international trade is affected by such practices.

EMPIRICAL REVIEW ON LITERATURE

Customary points of view in macroeconomics, for instance, Keynesians approach emphasize the expansionary effects of debasing to yield and advancement. In this strategy yield is managed by aggregate hobby and corruption will have a gainful result by duplicating aggregate demand and yield. Deterioration has an expansionary sway through "utilization trading and diminishing effect". It can move the enthusiasm from remote stock to privately conveyed items (Taye, 1999). In addition, when there is debasing in a country the expense of imported items will increase while the expense of nearby stock will decrease which accordingly will extend the passage of items. Additionally, if the Marshall-Lerner condition is satisfied downsizing of cash can upgrade the trade evening out furthermore GDP as time goes on.[1]

Devaluing can secure advancement through changes esteem competition. (Harris, 2001) determined that debasing may moreover provoke higher advancement by the diminishment in relative firm's cost certainly influencing their advantages. As the cost of imported items manufacture, people will move to private stock. The assemble opportunity to the remote business part and the augmentation in the use of private as a delayed consequence of deterioration will lessen the cost of creation. For this circumstance, creators will give less costly cost that can engage them to extend their advantage and get the opportunity to be engaged in the business area and advancement.[4]

Devaluation can likewise be utilized as one method for stabilizing so as to expand development the economy by expanding fares and enhancing the present record too controlling overvaluation of the conversion scale that build import of products, (Branson, 1986).

Paul (2006) gave a backing to the constructive outcomes of devaluation on monetary development on firms that create both in the nearby and remote business sector. At the point when a money is devaluated the measure of benefit picked up by a firm delivering in the remote business, sector builds when changed over to the nearby coin. This increment in benefit can be utilized for the improvement of the R & D and additional advancements of new innovations. At long last the change and presentation of new advances through benefit will diminish their past expense utilized which as a part of turn build yield.

Additionally made a comparative contention with speculation. He included the increment in fare part and developments will prompt "speculation drove development". This ascent in ventures will bring about development in GDP, (Gala, 2007).

Devaluation of currency in a nation where there is a settlement of indexation may have a contractionary impact. At the point when the cost of products increment as a consequence of the depreciation of currency the genuine compensation will fall and makers will be compelled to expand the pay rate keeping in mind the end goal to make specialists accomplish economical rate of living expense. This will diminish the benefit of makers as their expense will expand, (Acar, 2000).

Despite its expansionary impact devaluing currency negatively affects the development of a nation. (Krugman and Taylor, 1978) specified depreciation will actuate an increment in benefits offer of GDP negatively affecting

[4] "According to the Marshall-Lerner condition, devaluation of currency will have a positive effect on trade balance if the sum of price elasticity of export and import is greater than 1" (Ratha, 2010)pp.249

total interest if the careful inclination of firms and capital proprietors is higher than for compensation workers.

For a nation that is profoundly needy in the non-tradable division degrading can have a negative effect. The dissemination of asset from the benefit picked up in the exposed segment to the non-exposed segment and the expense of cost for imported merchandise utilized for creation won't be corresponding. Because of this, the unexposed divisions and, in addition, the aggregate yield development will lose. (Goldberg, 1990; Stryk, Jr, and H., 2000).

Devaluation can bring about the high benefit for firms that are presented to the business sector. Be that as it may, now and again this high benefit will make firms unmoving if there is less rivalry, ideal circumstance lastly bring about no adjustment over the long haul. As indicated by the hypothesis of change firms will build their profitability and turn out to be more innovative when there is a high rivalry, sudden fall in the interest of items or an expand generation cost and result in a low benefit (Erixon, 2007).

Additionally, Studies demonstrate that the consequence of expected and unexpected devaluation may affect the long-run development rate. (Serven and Solimano, 1992) recommended that normal debasement can negatively affect the development of an economy. The increment in the deterioration of genuine conversion standard is one component for the increment in the financing cost. What's more, when financial specialists expect the ascent in the devaluation rate, they will not wish to contribute and this will hinder venture and hamper development over the long haul. Courchene (2002) additionally included foreseen devaluation will diminish the rate of innovation and debilitate advancement in investment as financial specialists expect the increment in the cost of imported inputs. Though when organizations don't expect to devalue they won't concern anything so they will contribute and it won't have an impact on the investment rate, (Serven, 1990).

CASE STUDY

THE IMPACT OF YUAN DEVALUATION ON GLOBAL CURRENCIES

The fall in China's Yuan in August middle two weeks from 7th to 21st has drastically trebled the FX markets drastically, having a major impact on emerging economies. Keeping in mind the apparent risks of currency wars due to this China has had a goof trading relationship with Latin America, where Latin American companies exported raw materials to Chinese firms to manufacture products at lower costs, which could then be sold back to Latin *devaluation, the decline in Chinese Yuan has drastically affected the Asian countries who were major exporters to China. These economies now faced even greater completion in the international markets, who were struggling to gain the upper bound of their export volumes and price revenues.* The Latin American countries were also affected by this devaluation policy. This devaluation also affected China's own imports, which became relatively expensive to its exports. China was trying to develop and boost its domestic automobile industry with this devaluation. The prices for crude oil also decline following lowering growth of the industries and imports of oil by China due to the higher cost of importing goods with a devalued Yuan.

Most of the exporters of oil are the Middle Eastern countries. They were, thus, also affected by the Yuan's devaluation, resulting in pressures on development n these economies. The developed countries, however, have gained from the devaluation of the Yuan, with their currencies pegged to the US Dollar, unlike the currencies for commodities like The Canadian and Australian Dollar, which declined in value against the USD, *(Meyer, 2015).*

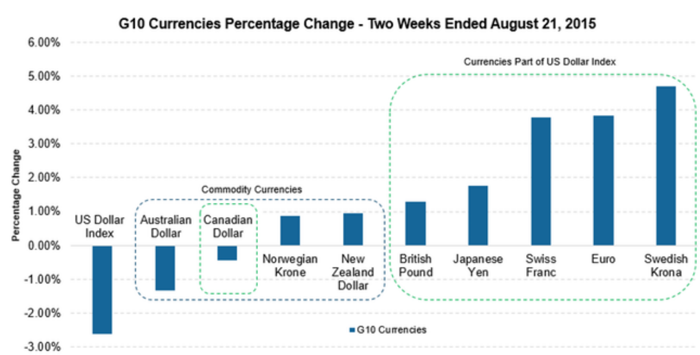

Figure 2: Source: Market Realist

Market Impact

There was a negative impact on the American Depository Receipts (ADRs) which were being traded globally during the week from 7th to 21st August 2015. Sony (SNE) declined by 8.64% while Exxon Mobil (XOM) and BHP Billiton fell by 6.11% and 10.24% respectively, *(Meyer, 2015).*

Effect on Latin American Currencies

America. The strategic decision by China to devalue its currency for the purpose of boosting domestic growth and restricting imports will adversely affect all such countries, which relied on selling goods and services to China.

Impact on Mexico, Columbia, and Brazil

Mexico and Columbia being the major exporters of crude oil to Chine has face declined in their GDP due to Yuan's devaluation.

The Chilean Peso has been adversely affected by the Yuan's devaluation as China was the major importer of Chile's copper produce. The Brazilian Real, however, gained positive signals with the avoidance of the Brazilian President's prosecution, thus preventing the country to be rated as a 'junk investment arena'.

Market Impact

The EFTs in the Latin American markets have shown a poor performance during the period of 7th to 21st August 2015. The iShares of MSCI Brazil Capped ETF and Latin America 40 ETF (ILF), both declined in value by 6.27% and 8.60%, respectively.

The American Depository Receipts (ADRs) have been impacted by the devaluation of the Chinese Yuan in the South American trading region. It had a very drastic impact Cemex (a construction company) and major oil and construction companies in Mexico, Brazil and Colombia (Petroleo Brasileiro Petrobras (PBR) and Ecopetrol (EC)) declined in value by 18.42%, 12.89%, and 7.94% respectively, *(Meyer, 2015)*.

Reaction to Yuan's Devaluation by the EMEA Countries

The EMEA (Europe, the Middle East, and Africa) countries have reacted in a mixed manner to the devaluation of the Chinese Yuan. The EMEA's European subgroup can be divided into two further categories; (i) the ones with strong reaction with the European Union (EU) and, (ii) the ones whose connections are more inclined towards Russia.

The countries which have their currencies pegged with the Euro will experience a boost in their economies due to their strong links with the Euro. The countries which have a greater deal of business with Russia will be impacted more due to falling in the value of the Yuan. This impact would be even greater with the falling crude oil prices and Ruble's depreciation. While in the Middle East, where exchange rates are controlled by the central bank's operations, only a few currencies are under pressure from Yuan's depreciation. The African countries, whose currencies are pegged in some way or the other are also under pressure to remove the pegs due to the Yuan's depreciation, *(Meyer, 2015)*.

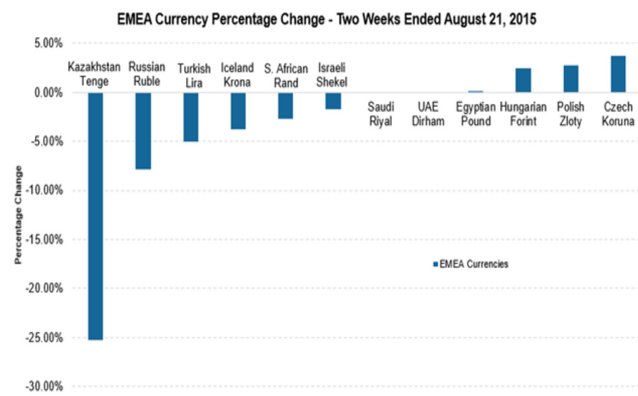

Figure 3: Source: Market Realist

Who Gained and Lost?

The movement of the EMEA currencies within the 7th to 21st August week is being displayed in the graph above. Those countries to whom China was a major importer, like crude oil lost the currency game due to the devaluation of the Yuan with the further pressure of globally decreasing oil prices.

The Kazakhstani Tenge have experienced the greatest impact of this devaluation because its central bank was following a floating exchange-rate policy. Kazakhstan lost this currency war due to ever falling crude oil prices with the back0toback devaluation of its major trading countries' currencies like China and Russia. Czech Koruna and the Polish Zloty have gained during this currency war due to their currencies' pegging with the Euro.

Market Impact

Moving over to the Asian Exchange-Traded Funds (EFTs) in the emerging economies, the iShares of MSCI South Africa (EZA) declined by 11.55% along with the fall in the value of MSCI Turkey ETF's (AAXJ) iShares, which was down by 12%, during August 7th to 21st, 2015.

The EMEA American Depository Receipts (ADRs) of Turk cell Iletisim Hizmetleri AS (TKC) declined by 10.53%. Similarly, prices of African ADRs like Sasol (SSL) and Russian ADR MobileTelesystems (MBT) fell by 11.29% and 14.02% respectively during the same period, (Meyer, 2015).

Decline in Asian Currencies when the Currency War Risk Increases

The Asian currencies have shown a decline in value during August's week from 7th to 21st, 2015. This reflected a continuous fall in the price/value competitiveness in Asian goods unless they deliberately lower their exchange rates. Speculations are that this may result in an upsurge of currency war within the Asian region, *(Meyer, 2015)*.

By the second week in August, when the Yuan gained stability, the currencies wars seemed much less likely for the time being. These currencies were already under pressure of due to the misrepresentative economic indicator of China, even before the Yuan was devalued.

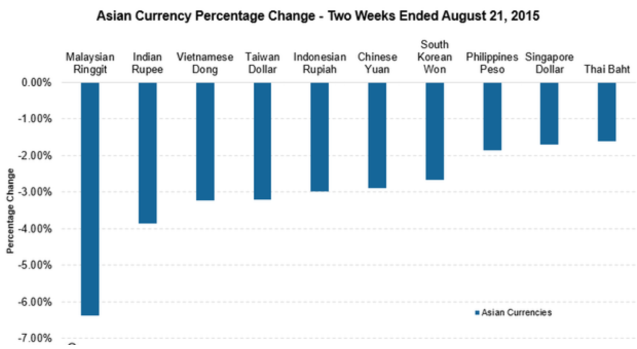

Figure 4: Source: Market Realist

Relative Impact on Currencies

The graph above portrays the impact on Asian region currencies, which showed a continuous decline in value till 21st of August, 2015. This fall, especially the drastic decline in the Malaysian Ringgit, partially engined by the devaluations of the Chinese Yuan, along with indirect factors such as the decline in crude prices which adversely affected energy exports of the country.

The Indian Rupee, which had usually remained stable due to its stable Foreign Exchange reserves, also experienced a fall in its value, to its lowest in the two years.

Thailand's Baht only fell by 0.36% in August's first week. In the following week, the sharp decline was due to the bomb attack in Bangkok, which devalued the Baht by 1.26%. Further, the currencies low liquidity in the money markets seems a possible explanation for its strong currency position among other Asian currencies. Most Asian currencies felt the high pressure of the devaluation shocks with the Malaysian and Vietnam governments taking deliberate steps to devalue their currencies in response to currency wars, through their central banks, while some currencies were affected by market movements and pressures, *(Meyer, 2015)*.

Market Impact

Moving over to the Asian Exchange-Traded Funds (EFTs) in the emerging economies, the SPDR S&P EFT (GMF) declined by 10.57% along with the fall in the value of MSCI All Country Asian ex-Japan ETF's (AAXJ) iShares, which was down by 8.45%, during August 7th to 21st, 2015.

In the goods industry, among the major portion of the American Depository Receipts (ADRs), shares of Infosys Limited (an Indian Software company) declined by 2.73%. Similarly, prices of Philippine Long-Distance Telephone (PHI) and Alibaba (BABA) fell by 4.18% and 13.49% respectively during the period.

Future of Emerging Countries

The countries which are heavily dependent on exporting primary commodities and manufactured items seem to be looking ahead towards turbulent times. The central banks are becoming responsible for controlling the monetary policies and pegging exchange rates within Asia's continent. In the era of increased competition and boundary-less trade among countries, inflexible functional strategies may undermine the countries' growth rates.

Since the emergence of carry trade[5] between the developing nations and the European markets, there has been a significant outflow of profits from developing nations to the developed countries. This carry trade became, even more, beneficial to the European currency holders due to the further decline in the value of the Euro. Currently, the investors are extracting their investments out from the developing nations to pay back the loans they have taken, thus raising the value of the Euro again due to increased demand for the currency, (Meyer, 2015).

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[5] Carry Trade refers to a strategy of purchasing an asset that is expected to provide high expected returns from the money borrowed at lower interest in another market. This spread between low cost of borrowing and purchasing an asset of higher expected rate of returns enable an investor to gain profits. This strategy is very common the FX markets.

Figure 5: Source: Market Realist

Risks in Other Currencies

The central bank of Egypt has maintained the exchange rate of the Egyptian Pound at 7.73/USD. The strategy behind this was to let the exchange rate devalue in a controlled way. Other currencies, such as Nigeria's Naira, whose values are pegged to the US Dollar are also following the same strategy. The competitiveness of the manufacturing business of these countries, however, might suffer, if these currencies do not devalue as per planned against the US Dollar.

The over-reliance on a specific commodity or industrial sector has also led to these risks. Keeping in mind the era of declining global prices in oil, oil-exporting countries, who have pegged their currencies with the US Dollar, especially the Saudi Riyal and the UAE Dirham, will be hurt if they decide to devalue their currencies. Staying with the discussion, the *Kazakhstani Tenge declined by 25% in its value with the second and third week of August from the 7th to 21st at the close.*

The UAE has taken a good strategic step to diversify its investments in other sectors like tourism and construction, thereby decreasing its heavy dependence on oil reserves only. The Hong Kong Dollar also faces similar pegged-currency risks in its exported goods and services, (Meyer, 2015).

Effect on the Market

Moving over to the Exchange-Traded Funds (EFTs) in the emerging economies, the iShares of MSCI EFT (EEM) declined by 9.77% along with the fall in the value of Vanguard FTSE EFT (VWO), which was down by 9.80%, during August 7th to 21st, 2015.

In the manufactured goods industry, among the major portion of the American Depository Receipts (ADRs), shares of South Korean LG Display declined by 12.28%. Similarly, prices of Taiwan Semiconductor Manufacturing (TSM) and Semiconductor Manufacturing (SMI) fell by 10.22% and 4.72% respectively during the period, (Meyer, 2015).

CONCLUSION

Currency devaluations is a strategic attempt to attain the economy policy. It helps to put up exports by weakening the currency relative to the rest of the world. It also contracts the trade deficits and favors the government to overcome its outstanding debts by reducing the costs of interest payments. However, there are also some cons. They make asset market to fall by creating uncertainties in global markets. Also, the countries may indulge into a 'tit for tat' war which can be devastating cycle bringing no good to economies.

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