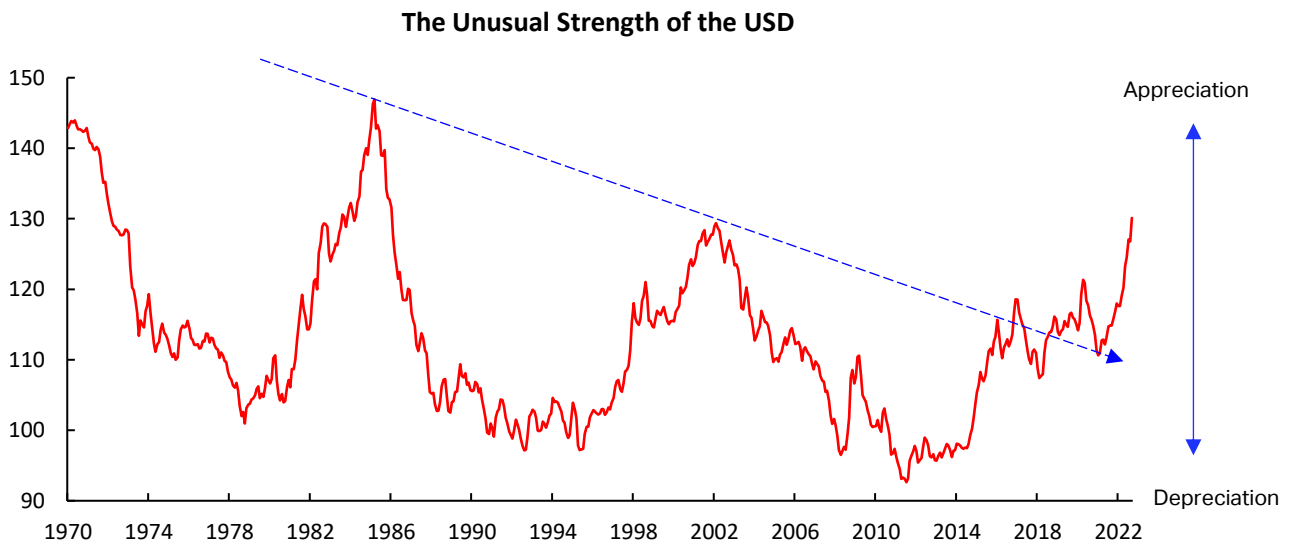




## IATA Economics' Chart of the Week

14 October 2022

### The unusual strength of the USD adds to airlines' burden



Source: JP Morgan, Macrobond.

Note: The red line represents monthly J.P. Morgan Real Broad Effective Exchange Rate Index for US dollar, with 2010 = 100.

- The US dollar can be characterized as a trend-depreciating currency, setting progressively lower highs, as can be seen in the chart above. However, since the beginning of 2021, the currency has seen a sharp appreciation, the pace of which has accelerated during the course of this year. Adjusted for relative price levels and weighted according to countries' share of US trade, the chart shows the broad real effective exchange rate of the dollar. In September this index reached 130.1 - a level not seen since 1986. That is up from 110.6 in January 2021 and an appreciation of 17.6% since that time.
- The US dollar is a "safe-haven" currency which tends to benefit from any turmoil around the world, even when such turmoil originates in the US. This phenomenon was described by the economist Barry Eichengreen as the "exorbitant privilege" of being the issuer of the world's reserve currency. The accelerated appreciation of the US dollar in 2022 is first and foremost linked to the war in Ukraine. This war, in turn, is a major cause behind the surge in inflation, leading numerous central banks, including the US Federal Reserve, to raise nominal interest rates. Higher interest rates make the US dollar even more attractive to investors, adding to the safe-haven effect at this particular point in time.
- For airlines, the stronger US dollar adds another layer of cost, on top of high inflation in general and high jet fuel prices in particular. All US dollar-denominated costs rise for everybody whose revenue is in another currency. Similarly, the debt burden increases for all non-dollar-based entities who have borrowed in dollars. In addition to fuel, which tends to be invoiced in US dollars, this is very much the case for aircraft as well, for instance. US-based airlines, on the other hand, will be spared this double whammy, and any non-USD-denominated costs they might have will be reduced by the effect of the stronger US dollar.
- The silver lining that we can find in this cloud is that the US Federal Reserve will arguably not need to raise their policy interest rates by as much as might otherwise have been the case, given that significant monetary-policy tightening is being delivered through the currency appreciation. The rest of the world though, finds itself in the opposite situation, likely having to tighten by more to stave off imported inflation as their currencies weaken.

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