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China's Hu Buys Time at G-20 With Yuan Announcement

By Bloomberg News - Jun 21, 2010

Chinese President Hu Jintao will meet with world leaders at the June 26-27 Group of 20 leaders' summit. Photographer: Nelson Ching/Bloomberg

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June 21 (Bloomberg) -- Nicholas Lardy, a senior fellow at the Peterson Institute for International Economics in Washington, talks with Bloomberg's Rishaad Salamat about China's shift in currency policy, and its implications for the nation's economy and trade. The People's Bank of China two days ago indicated it's abandoning the 6.83 yuan peg to the dollar adopted during the global crisis to shield exporters. The central bank said while there's no basis for "large scale" moves in the currency, the exchange rate will be allowed increased "flexibility." (Source: Bloomberg)

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June 21 (Bloomberg) -- Komal Sri-Kumar, chief global strategist at TCW Group Inc., talks with Bloomberg's Rishaad Salamat about the impact of a change in China's currency policy. The People's Bank of China two days ago indicated it's abandoning the 6.83 yuan peg to the dollar adopted during the global crisis to shield exporters. The central bank said while there's no basis for "large scale" moves in the currency, the exchange rate will be allowed increased "flexibility." (Source: Bloomberg)

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June 21 (Bloomberg) -- Bloomberg's Stephen Engle reports on China's currency policy, and implications for the nation's economy and global trade. China’s signal of an end to the yuan’s fixed rate to the dollar may accelerate a shift toward domestic demand as the prime driver of growth as President Hu Jintao seeks to strengthen household incomes. Bloomberg's Rishaad Salamat also speaks. (Source: Bloomberg)

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June 21 (Bloomberg) -- Andrew Colquhoun, director at Fitch Ratings Asia-Pacific sovereign group, talks with Bloomberg's Rishaad Salamat about the outlook for Japan's credit rating and fiscal policy. Colquhoun, speaking from Tokyo, also discusses China's shift in currency policy, and its implications for the nation's economy. The People’s Bank of China two days ago indicated it’s abandoning the 6.83 yuan peg to the dollar adopted during the global crisis to shield exporters. The central bank said while there’s no basis for “large scale” moves in the currency, the exchange rate will be allowed increased “flexibility.” (Source: Bloomberg)

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June 21 (Bloomberg) -- Qu Hongbin, chief China economist at HSBC Holdings Plc, talks with Bloomberg's Haslinda Amin about China's currency policy. China said on June 19 it will allow a more flexible yuan, signaling an end to the currency’s two-year-old peg to the dollar a week before a Group of 20 summit in Toronto. Qu, speaking from Hong Kong, also discusses the outlook for China's economy and the nation's demand for U.S. Treasuries. (Source: Bloomberg)

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June 21 (Bloomberg) -- Ben Simpfendorfer, chief China economist at Royal Bank of Scotland Group Plc in Hong Kong, talks with Bloomberg's Haslinda Amin about China's yuan policy. China’s yuan climbed the most in 18 months against the dollar after the central bank signaled it would end a two-year peg. The People’s Bank of China said on June 19 it will allow greater “flexibility.” Yesterday, it ruled out “large changes” in the exchange rate and said it will prevent “excessive” moves. (Source: Bloomberg)

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June 21 (Bloomberg) -- Jim O'Neill, chief global economist at Goldman Sachs Group Inc., talks about China's relaxation of a two-year peg of the yuan against the dollar. He speaks with Andrea Catherwood on Bloomberg Television's "The Pulse." (Source: Bloomberg)

Chinese President Hu Jintao may have succeeded in removing the yuan's valuation from debate at this week's Group of 20 leaders' summit, economists and political analysts say. How much time he's bought depends on how flexible the currency will become.

Days before China's central bank announced on June 19 that the yuan's "flexibility" would increase, officials said the currency's value was not a suitable item for discussion at the G-20 meeting in Toronto. Hu will meet with President Barack Obama and other world leaders at the June 26-27 summit to discuss items ranging from the global response to the European sovereign-debt crisis to increasing the influence of developing countries in the International Monetary Fund.

U.S. lawmakers threatened to thwart China's wish to keep the yuan off the meeting's agenda. House Ways & Means Chairman Sander Levin, a Michigan Democrat, said on June 16 that China needed to act by the end of the summit or risk U.S. legislation which could levy penalties on Chinese imports.

"I think the announcement is in a sense preemptive and will probably keep currency off the agenda at the G-20 meeting, a well advertised Chinese goal," said Nicholas Lardy, a senior fellow at the Peterson Institute for International Economics in Washington. "My view is that they have at a minimum bought some time."

Yuan Rises

China's currency posted its biggest gain in 20 months in the first day of trading after the announcement. The yuan rose 0.36 percent to 6.802 per dollar as of 1:45 p.m. in Hong Kong, the biggest advance since Oct. 7, 2008, according to the China Foreign Exchange Trading System. The 12-month non-deliverable yuan forward rose 1.4 percent to 6.6209, implying traders are betting on a 2.7 percent appreciation.

Obama, in a statement, called China's decision a "constructive step." U.S. lawmakers said the move was insufficient.

Senator Charles Schumer, the New York Democrat who is co- sponsor of legislation that would allow for duties on Chinese imports, said he was dissatisfied with a statement that didn't indicate the timing or amount of adjustment.

"We hope the Chinese will get more specific in the next few days," Schumer said on June 19. "If not, then for the sake of American jobs and wealth, which are hurt every day by China's practices, we will have no choice but to move forward with our legislation."

'Concrete Actions'

Senator Charles Grassley of Iowa, the Finance Committee's ranking Republican, said the Obama administration and Congress "need to keep the pressure on until China takes concrete actions to appreciate its currency exchange rate in a meaningful way."

China's central bank yesterday reaffirmed it would maintain the yuan's 0.5 percent daily trading band and said greater yuan flexibility would help cut the trade surplus and reduce the reliance on exports as a driver of growth.

The yuan had been held at about 6.83 to the dollar since mid-2008. The currency appreciated 21 percent in the three years after a peg to the dollar was scrapped in July 2005 and replaced by a managed float against a basket of currencies including the euro and the Japanese yen.

The persistent surplus has been a driving force of Washington lawmakers' ire. China is the second-biggest trading partner of the U.S. after Canada and the U.S. is China's biggest single-country export market. Two-way trade last year amounted to $366 billion, with China recording a $226.8 billion surplus, according to U.S. Commerce Department data.

In 'Spotlight'

Should the yuan resume its appreciation against the U.S. dollar, which was suspended in July 2008 as world economic growth slowed, then China can "avoid becoming a target in the spotlight" at the G-20, said Li Cheng, head of research at the John L. Thornton China Center at the Brookings Institution in Washington.

That will allow China to focus on its own agenda at the meeting. Vice Foreign Minister Cui Tiankai told reporters on June 18 that China wanted to discuss new quotas for the IMF that would boost the power of developing countries, promote the overhaul of global financial regulations, speak out against trade protectionism and pay more attention to economic development in poorer countries.

Zhang Tao, head of the central bank's international department, said at the same briefing that Europe's sovereign debt crisis was also a high priority for discussion.

'Shifting Attention'

China, by moving on its currency ahead of the Toronto summit, has shifted attention to the budget deficits of developed nations, said Eswar Prasad, a senior fellow at the Brookings Institution and a former head of the China division at the International Monetary Fund. Vice Finance Minister Zhu Guangyao said June 18 that China's fiscal debt was about 20 percent of gross domestic product. That compares with almost 100 percent in the U.S.

Still, Hu's respite may be cut short if China's trade surplus rises and the yuan appreciates no more than 2-3 percent against the dollar in the coming months, Lardy said.

Reports this month from the U.S. and China highlighted concern that trade imbalances, which reached record levels before the global financial crisis, may be reemerging. Chinese exports climbed 48.5 percent in May from a year earlier. In the first four months of the year the U.S. posted a $71.0 billion trade deficit with China, up 5.7 percent from the year-ago period.

"China could come under renewed pressure," Lardy said.

--Michael Forsythe in Beijing, with assistance from Rebecca Christie and Ian Katz in Washington and Li Yanping in Beijing. Editors: John Brinsley, Paul

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