

Why the Yuan Is Rising

By [Bruce Einhorn](#) on October 26, 2012

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China's currency hit a 19-year high against the U.S. dollar on Friday. Not coincidentally, on the same day the yuan rose to 6.238 against the greenback, disgraced former Politburo member Bo Xilai suffered his latest indignity, with the official Xinhua News Agency announcing [his removal](#) from the National People's Congress, China's rubber-stamp legislature. "According to the law on deputies to the NPC and to local people's congresses," the NPC Standing Committee said in a statement, as reported by Xinhua, "his post was terminated."

The latest setback for Bo comes a month after he got booted from the Communist Party and is another sign China is back on track for the leadership transition set for early next month.

The yuan's rise is related to Bo's downfall because the uncertainty surrounding Chinese politics during the past six months has been one factor contributing to the currency's weakness. It wasn't that long ago that the significant pressure on the yuan was for it to go down, not up. Over the summer, China's leaders were distracted by the Bo Xilai scandal. Vice President Xi Jinping, the heir apparent to President Hu Jintao, disappeared from public view for two weeks last month. That only [added to worries](#) that China's leadership was too distracted to focus on economic issues.

Confusion about China's politics came at a time when the economy was struggling and China's exporters were feeling the heat from the global slowdown. Given that combination, "many people in the market expected significant RMB depreciation," Lu Ting, chief China economist at Bank of America ([BAC](#)), told Bloomberg Television on Oct. 18.

Now, with the trial of Bo's wife concluded, there's less reason to worry about what might happen when China's leaders gather for the Communist Party congress, which is scheduled to begin on Nov. 8. It's likely everything will now proceed as scripted, with Xi taking over as president and Vice Premier Li Keqiang replacing Wen Jiabao as premier.

Meanwhile, the Chinese economy is showing signs of recovery. Recent numbers for industrial production, fixed-asset investment, and retail sales have all surprised on the upside, leading some economists to say [the worst is over](#) for the world's No. 2 economy. Growth in factory output will pick up in the final quarter of the year, putting the country on track to meet its target of 7.5 percent, Zhu Hongren, chief engineer at the Industry and Information Technology Ministry, said on Thursday.

With the political uncertainty reduced and the economic picture improving, the yuan is on the rise again. The currency has strengthened more than 2 percent against the dollar over the past two months. "Earlier this year, people's worries about China's economy increased, which caused a decline in yuan demand," Steven Bell, a fund manager at London-based hedge fund GLC, [told Bloomberg News](#) on Thursday. "The trend of outflows has now reversed, and China will probably attract more inflows."

There's another reason the Chinese currency is on the upswing. China's leaders know both Democrats and Republicans in the U.S. have been hammering China over its currency, which they say is undervalued and hurting American exporters. Republican Mitt Romney says he would declare China a currency manipulator on Day One of a Romney administration.

Allowing the yuan to strengthen to a two-decade high against the greenback might be the Chinese government's way to show the Americans they aren't ignoring those concerns. The yuan's rise "helps China

head off criticism ahead of November's U.S. presidential election," Barclays ([BCS](#)) analysts Nick Verdi, Olivier Desbarres, and Hamish Pepper wrote in an Oct. 19 note.

Eswar Prasad, a Cornell professor and former IMF China head, argues the Chinese government has not been depressing the value of the yuan: "Right now it's hard to make the case that China is manipulating its currency," he told Bloomberg TV on Oct. 23. "The RMB has appreciated, and they have allowed for more flexibility." If Romney wins, Prasad expects him not to follow through on his threat to go after China's yuan policy on Day One of his presidency. "The currency manipulation charge is something Romney is going to have to walk back from if he is elected," said Prasad.

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