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Tensions trouble Seoul as summit looms

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Japan's polite but pointed call for currency responsibility from South Korea and China has highlighted growing **international tensions** over exchange rates ahead of a **summit of the G20** leading economies in Seoul next month.

Tokyo had previously refrained from even implied criticism of Seoul over currency issues, despite what traders say is the Bank of Korea's role in ensuring a cheap won that has given Korean exporters a big edge over their Japanese rivals.

That Naoto Kan, Japan's prime minister, is willing to point a finger at South Korea will be seen as a further sign that G20 ministerial and leaders' gatherings will be – as Nomura analysts declared recently – "the next major confrontation in the global **currency wars"**.

Such a prospect will be worrying to Seoul, which is this year's G20 president and is sensitive to accusations it fixes exchange rates to help politically powerful conglomerates.

Traders say interventions have been "substantial" and "aggressive", with the Bank of Korea often buying more than $1bn each day – with the result that foreign exchange reserves have hit all-time highs in recent weeks.

The won is the only main Asian currency to have dropped in value against the dollar since 2008, in sharp contrast to the Japanese yen and Australian dollar which have both climbed more than 20 per cent.

The South Korean government, which has allowed the won to appreciate 8 per cent against the dollar in the past three months, says it only intervenes to smooth excessive volatility and never tries to buck the overall market trend.

But Mr Kan's comments in the Diet on Wednesday suggest such arguments may not be enough to shield Seoul from criticism ahead of the G20 gatherings. Tokyo appears keen to shift international attention away from its own foreign exchange market intervention last month, launched to try to stem a rapid rise in the yen that officials fear could derail the economy's fragile recovery.

Far greater pressures are likely to be applied to China. Data released on Wednesday showing a record jump in China's enormous foreign exchange reserves and stubbornly high trade surplus will provide fresh ammunition for trade partners that accuse China of protectionist currency undervaluation.

"China is keeping down the renminbi's value and helping to prop up the US dollar, both of which run counter to the long-term adjustment needed in the global economy," according to Eswar Prasad, former head of the IMF's China division and a professor of trade policy at Cornell University.

"China's growing reserve stockpile and the policies underlying it are a prominent indicator of the fissures opening up between national and collective interests," Prof Prasad says.

While the US has led such criticism, other countries have joined in in a more muted way.

Rainer Brüderle, German economy minister, who is visiting China, was quoted on Wednesday as saying Beijing should make concessions to avoid turning tensions into a damaging trade war. "China bears a lot of the responsibility for avoiding an escalation," Mr Brüderle told Handelsblatt newspaper.

Beijing has responded to increasing pressure by allowing the renminbi to appreciate against the dollar at a slightly faster rate in recent weeks.

But in statements released on Tuesday, China's State Administration of Foreign Exchange tried to damp expectations of a rapid renminbi rise.

Some emerging markets have argued it is the prospect of yet looser monetary policy in the US, as much as the Chinese manipulation of their exchange rate, that is creating destabilising capital flows.