China Lets Currency Weaken, Risking New Trade Tensions

By KEITH BRADSHER

HONG KONG — China’s currency dropped further in May against the dollar than in any other month since the Chinese government began allowing the renminbi to appreciate gradually in the summer of 2005. The shift could help Chinese exports but worsen trade friction with Europe and particularly the United States.

By setting weaker and weaker daily “fixings” for the renminbi against the dollar at the start of each day’s trading, China’s central bank has pushed down the renminbi 0.9 percent against the dollar over the last month. The decline in the daily fixings coincides with signs that the Chinese domestic economy is slowing sharply this spring and may need help from stronger exports.

A cheaper renminbi makes Chinese exports more competitive in overseas markets while making foreign goods more costly and less affordable in China. The Obama administration has been pressing China for the last three years to allow faster appreciation in the renminbi, not depreciation, as a way to narrow the United States’s trade deficit with China, which reached a record $295.46 billion last year.

The Treasury Department issued a report last Friday criticizing China’s management of its exchange rate and calling for the first time for China to release data on the scale of its foreign exchange market interventions. But the report stopped short of labeling China a currency manipulator, a label that Chinese leaders have indicated they would bitterly resent and oppose.

The Chinese central bank pushed the renminbi up slightly on Monday, the first trading day after the Treasury report, but has let it slide further each of the last three trading days. The Treasury declined on Thursday to comment on the renminbi’s depreciation while the Chinese central bank, the People’s Bank of China, has stayed silent this spring on currency policy.
Mitt Romney, the presumptive Republican presidential nominee, said last autumn that if he were elected president, he would label China a currency manipulator on his first day in office. One of his recent television ads predicts the expected actions of Mr. Romney’s first day in office, with the narrator saying that through the day, “President Romney stands up to China on trade, and demands they play by the rules.”

Bankers and economists say that there have been some hints that foreign investors and Chinese citizens alike have been moving money out of China in recent weeks, which could have contributed to the fall in the renminbi. Money managers around the world have become more risk averse as the European and Chinese economies have deteriorated this spring, setting off a decline in the currencies of many emerging markets.

China has also been bothered by political worries this spring associated with the purge of Bo Xilai, who was suspended from the Politburo in April.

But with more than $3.3 trillion in foreign exchange reserves, combined with tight regulatory controls on the Shanghai currency market and some lingering controls on the movement of money in and out of China, Beijing still has great discretion in deciding the daily value of the renminbi. While Chinese officials have been silent about currency policy in recent weeks, few economists doubt that the recent decline in the renminbi represents anything other than an attempt to stimulate exports.

“During a difficult period of slowing growth and weak export demand, the government is taking the opportunity afforded by an apparent net outflow of capital to guide the value of the renminbi lower against the dollar to help support exports,” said Eswar S. Prasad, a former China division chief at the International Monetary Fund.

The Chinese economy is suffering this spring from the slowest fixed-asset investment in a decade, steadily declining foreign investment, weakening retail sales and a rapidly deflating real estate bubble. China could benefit considerably from the jobs and wealth that would be created by ramping up exports and supplying a larger share of the world’s demand in markets, ranging from shoes and garments to flat-panel displays and auto parts.

But a surge in Chinese exports in the middle of a global economic slowdown could also ruin the livelihoods of large numbers of workers in other developing countries that compete with China to supply the same goods.

China is also shifting its exports toward higher-technology products like telecommunications gear and power plant turbines. So an expansion in Chinese exports could also displace...
sizable numbers of workers in the United States, Europe and Japan who produce goods similar to those from China.

China may have another motive in allowing the renminbi to decline against the dollar over the last month: the dollar’s strength. The euro has been sliding against the dollar this spring, and because the renminbi is effectively linked to the dollar, the euro has also been weak recently against the renminbi.

This has hurt the competitiveness of Chinese exports to Europe — and China exports slightly more to Europe than it does to the United States. Even with the renminbi’s decline against the dollar in May, the renminbi still rose 5.5 percent against the euro during the month.

A few Chinese economists are even arguing that the renminbi should now be devalued further. They are largely ignored by mainstream Chinese economists but are starting to receive a warm reception from some of the more nationalistic media outlets, like The Global Times, which is affiliated with People’s Daily and is stridently critical of the West and most of China’s East Asian neighbors, with the exception of North Korea.

Lu Zhengwei, the chief economist of the Industrial Bank in Fuzhou, is among the advocates of a weaker Chinese currency. “I personally think the renminbi will be more or less stable this year, but ideally, it should depreciate by at least 3 to 5 percent,” he said in an interview last Friday.

Mr. Lu said that Chinese exports to the United States, Europe and Japan were growing more slowly than these markets’ overall imports. “Thus sluggish overseas demand is not the only reason behind the slowdown of China’s exports — the appreciation of the renminbi’s effective exchange rate also contributed to it,” he said.

But many Chinese economists are skeptical of this argument, pointing out that a weak currency will keep the country dependent on exports and will keep prices of imported goods high for China’s long-suffering consumers. A lower economic growth rate in China is inevitable because the government is clamping down on the country’s large real estate sector, and should not be offset by government assistance to exporters through the currency market, said a senior Chinese economist who insisted on anonymity because he did not want to become embroiled in the public debate in China over currency policy.

Xu Yan contributed research from Shanghai.
China Lets Currency Weaken, Risking New Trade Tensions - NYTimes.com

6/1/2012

http://www.nytimes.com/2012/06/01/business/global/china-lets-its-currency-slip-raising-tra...