



Develop with the technologies you already know

I KNOW A PLACE THAT'S BRAND NEW, BUT FAMILIAR

GET STARTED

Windows Azure

THE GLOBE AND MAIL

February 19, 2010

China finds new ways to buy U.S. debt

By BRIAN MILNER

From Friday's Globe and Mail

Anonymous purchases made through unconventional channels would allow Chinese to remain biggest holders of American bonds

Despite a sharp reduction in its official stash of U.S. Treasuries, China is far from bailing on the world's safest and deepest market, analysts say.

Indeed, China may be adding to its vast hoard through secret purchases made through foreign banks. Such transactions do not show up in the U.S. data.

Such anonymous deals through intermediaries are common in the bond world, but they make it difficult to accurately assess whether a government is changing its core strategy, analysts say.

"We do not believe that the Chinese are dumping Treasuries," Arthur Kroeber, managing director of GaveKal Dragonomics, a Beijing research firm, told Associated Press. "What they are doing is diversifying the channels through which they make these purchases so that it is much more difficult for the market to ascertain what they are doing."

The U.S. Treasury identifies only the country of origin of the direct purchaser of its securities. So any bonds acquired through London, for example, would show up as a sale to Britain.

But the latest public numbers do signal a marked change in Beijing's pattern of investment.

"There's something going on here that we can't fully track, based on these numbers," said Eswar Prasad, a senior fellow with the Brookings Institution in Washington.

U.S. data show that China reduced its holding of Treasury bills in December by \$34.2-billion (U.S.) - a 4.3-per-cent decline - which pushed it into second place behind Japan as the largest foreign holder of U.S. debt.

But the Chinese increased their holdings of longer-term U.S. government bonds, even though rates at the long end of the yield curve are expected to rise.

"It's a little odd for the Chinese to be getting rid of short-term U.S. Treasuries and buying long-term bonds right now," Dr. Prasad said.

Such a shift makes some sense, because short-term notes are paying virtually nothing, while 10-year bonds carry close to 3-per-cent interest. "But the Chinese have expressed a lot of concerns about the high levels of U.S. debt and

deficits," Dr. Prasad said.

It would make more sense to wait for a year and see what happens to rates, he said.

Last year, China directly sold a net total of about \$95-billion worth of short-term T-bills and bought about \$124-billion of longer-term Treasury bonds. They also sold about \$25-billion of agency debt - securities issued or guaranteed by the two big U.S. mortgage-financing agencies, Fannie Mae and Freddie Mac - and bought about \$12-billion worth of equities and other U.S. bonds.

Add the numbers and it comes to an "implausibly small" level of about 3 per cent of net accumulated reserves, said Dr. Prasad, who is the former head of the International Monetary Fund's China division.

In previous years, the net total has bounced between 30 and 65 per cent.


"What we may be seeing is an intensification of their diversification strategy," he said. "Right now, they may just be picking up the pace of that a little bit."

The Chinese have made no secret of their desire to reduce their vast holdings of dollar-denominated instruments. But their options are limited, and continuing economic and financial woes in Europe and Japan narrow these even further.

As well, China's export-driven growth model and desire to keep a lid on its currency "almost certainly means that they're going to continue accumulating a lot of reserves," Dr. Prasad said.

The U.S. Treasury market is the only one capable of absorbing Chinese volumes. "Much as the Chinese would like to diversify away from the dollar, the reality is that they're stuck with U.S. Treasury bonds for a long time to come," Dr. Prasad said.

CTVglobemedia Publishing, Inc

 CTVglobemedia Publishing Inc. All Rights Reserved.. Permission granted for up to 5 copies. All rights reserved.
You may forward this article or get additional permissions by typing http://license.icopyright.net/3.8425?icx_id=/icopyright/?artid=1473812 into any web browser. CTVglobemedia Publishing, Inc and Globe and Mail logos are registered trademarks of CTVglobemedia Publishing, Inc . The iCopyright logo is a registered trademark of iCopyright, Inc.