

IMF chief looks to press China harder on yuan



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By Lesley Wroughton

WASHINGTON, June 27 - Frustrated that efforts to convince China to let its currency rise faster have fallen short, the head of the International Monetary Fund has told directors of the fund's board he wants a meeting to discuss the issue.

IMF Managing Director Dominique Strauss-Kahn privately tried to nudge the Chinese into making a substantial adjustment in the value of the yuan in Beijing in February to fend off pressure from the United States and increasingly disgruntled European countries.

Unable to make progress, the former French finance minister hopes that a meeting to specifically discuss China's currency will increase pressure on Beijing to heed to international calls to let the yuan rise at a faster rate, board directors say.

The board is made up of 24 directors who represent the IMF's 185 member countries and oversees the day-to-day decision-making at the institution, although it does not set policy.

In Cancun, Mexico, this week, Strauss-Kahn called the Chinese yuan "substantially undervalued" -- a rhetorical step beyond his previous calls for a further, faster rise.

His predecessor at the IMF, Rodrigo Rato, came under heavy fire from the U.S. Treasury and lawmakers for not pressing China hard enough on the currency front. Washington has long argued that an undervalued yuan gives Chinese producers an unfair advantage in global markets.

U.S. pressure has appeared to have eased somewhat in recent months, partly because the yuan's rise against the dollar has accelerated. On Thursday, it hit its highest level against the dollar since China dropped a dollar peg and revalued the yuan in July 2005. In all, it has risen about 20 percent.

European countries, on the other hand, are now pushing hard for China to act on its currency, and as a European, Strauss-Kahn is under pressure, board directors say. In sharp contrast to its movement against the dollar, the Chinese currency has depreciated by 7 percent relative to the euro since July 2005.

BEIJING PUSHES BACK

China has pushed back against the IMF's heavy prodding.

Last year, the IMF changed its currency surveillance rules to say that -- in addition to avoiding currency manipulation and intervention -- member countries should stay away from policies that result in "external instability."

Beijing said the rules were crafted to aid Washington's argument that the yuan is undervalued and has stalled the IMF's 2007 report on the Chinese economy, partly to make a point that it is seeking even-handed treatment by the fund.

An IMF staff mission was scheduled to visit Beijing several weeks ago to begin consultations with China for 2008, even with the 2007 report still not concluded. Beijing, however, told the IMF to delay the visit and rescheduled for last week, when top Chinese financial officials were in Washington for talks with the United States and not available to talk with the IMF.

"It was fairly clear they are continuing to play the game and not going to be very serious about the consultation," an IMF source said.

There is growing concern within the IMF that a rebalancing of the world economy is being slowed by an uneven currency adjustment -- with larger declines by the U.S. dollar against free-floating currencies, such as the euro, and smaller moves against currencies of countries with large current account surpluses, such as China.

"It is unclear how this will ultimately play out," said Eswar Prasad, an economics professor at Cornell University and a former IMF official, adding it would set a bad precedent for the future if China was allowed to opt out of the IMF's surveillance of the global financial system because the messages for Chinese policy makers may be harsh.

Prasad said the IMF's ability to conduct effective surveillance would be severely compromised if an important member, such as

China, was allowed to disregard standard IMF procedures, including annual economic consultations.

"The Chinese have boxed themselves into a corner -- with inflation well above their comfort zone, they should raise interest rates, allow the exchange rate to appreciate or do both," he said, "But they can't raise interest rates because that would bring in more capital inflows and lead to a lot more pressure on the exchange rate."

Prasad said there were no easy answers. "They have to start somewhere, rather than let the problem fester and risk even higher inflation in the future."

"Currency appreciation is by no means a panacea, but it is certainly part of the solution."

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