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## Donald Kohn Says China Will Need to Grant Independence to Its Central Bank

By Ian Katz - Feb 7, 2012

[Donald Kohn](#), a former vice chairman of the [Federal Reserve](#), said “the Chinese will need to allow the exchange rate to fluctuate.”

“They’ll need to grant independence for the People’s Bank of [China](#) to run an independent monetary policy aimed at macroeconomic stability,” Kohn said during a panel discussion at the [Brookings Institution](#) in Washington today. He is now a member of the Bank of England’s Financial Policy Committee.

The Obama administration says China uses an [undervalued currency](#) to give its exporters an unfair advantage in overseas markets. The U.S. Treasury Department, in a December report, called for China to adopt “greater exchange-rate flexibility.”

Chinese Vice President [Xi Jinping](#), who is set to become the next general secretary of the Chinese Communist Party later this year and to succeed [Hu Jintao](#) as president in March 2013, is scheduled to visit Washington next week.

For China, allowing the yuan to fluctuate would be preferable to higher wages and prices, Kohn said. Inflation in China may drop to as low as 3.2 percent in February from 6.5 percent in July, Bank of America Corp. forecasts.

The yuan advanced 0.1 percent today to 6.3048 per dollar in Shanghai. The People’s Bank of China set the reference rate at 6.3116 per dollar. The yuan, which advanced 4.7 percent in 2011, is little changed this year, according to data compiled by Bloomberg. The currency is allowed to trade 0.5 percent on either side of the daily fixing.

### Reserve Currency

Eswar Prasad, a senior fellow at Brookings and a professor of trade policy at [Cornell University](#) in Ithaca, New York, said the yuan will become a reserve currency held by many governments over

the next 10 years.

The Chinese currency “will erode the dollar’s dominance but will in no way displace it,” said Prasad, who presented a paper on the yuan’s role in the global monetary system.

[Stephen Roach](#), non-executive chairman of Morgan Stanley Asia, said he is concerned that both Republican and Democratic lawmakers are blaming China for U.S. unemployment.

The U.S. had trade deficits with 88 countries in 2010, proving that it has a “multilateral problem” that can’t be fixed by adopting measures against China, Roach said on the panel.

The U.S. trade gap with China in November declined 4.3 percent to \$26.9 billion. Exports to China climbed to the highest since December 2010, showing sustained demand from the nation for U.S.-made goods. The U.S. [trade deficit](#) with all countries increased 10.4 percent to \$47.8 billion in November, according to the Commerce Department.

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