

Rmb appreciation on chinas import and export economics essay



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Introduction

Money is an important factor in peoples life. Similarly, the currency also plays a significant role for the countries economy , particularly for the import and export trade among the countries.

The exchange rate is an important factor for economic balance adjustment in an open economy, the exchange rate policy not only can be used to adjust trade flow and trade balance, but also can be used to adjust the trade structure. Historically, the developing country normally use the depreciation currency as the competitive advantage in the early stages of development. However, the exchange rate adjustment on the import and export trade is conditional, whether the change of exchange rate can affect trade or not which depend on rate transmission mechanism. China has been focusing on the role of the exchange since its reform and opening up, after several major exchange rate adjustments, exchange rate movements has been an important role to reverse the trade deficit and change the unfavorable situation of trade in china.

In recent years, most of the countries were carrying on the exchange rate reform, adjusting the domestic currency on the foreign exchange rate, seeking some more development opportunities for the country's economy and the import-export trade. As we know, China's currency-RMB plays a significant role in the world's economy.

On July 21, 2005, the Chinese government announced on the exchange rate system will be reformed, abolishes the exchange rate system which fixed on u. s. dollar, and implements the management floating exchange rate system.
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From October 31, 2007, the RMB changed exchange rate against US dollar revalued from 8.1100 to 7.4692 at the same day which announcement of the reformation of exchange rate, until to the record low 6.7899 recently, RMB has experienced many transformations in the several years. At the same time, the RMB appreciation has also had many influences to chinese people's normal life.

For several years, people always discuss the advantages and disadvantages of exchange rate reformation, especially for the potential influence of the china's import and export trade., for example: textile, clothing, toys which is labor-intensive and meager profit. So far, exchange reform had been through more than two years, there was a lot of influence for each aspect of chinese economy caused by exchange reformation. This article will studies the reasons for the RMB appreciation and the development of china's import and export trade, and discuss the influence and solution of RMB appreciation on china's import and export trade.

Chapter 1 The overview and relationship with the RMB appreciation and import and export trade

The RMB appreciation, it means the Yuan's exchange rate against foreign currencies has been decreased. In recent years, china has been through continuous adjustment of RMB exchange rate policy to stimulate the RMB appreciation. Meanwhile, on the whole world situation, the exchange rate of dollar against euro is also increase continuously, and other countries' currency rate have also been adjusted during these years.

Import and export trade is a business which different countries (and/or region) exchange different goods and services with each other. Import and export trade is the international transfer of goods and services. Import and export trade is composed by two parts of the import trade and exports trade. Import and export trade is a country's trade method of external sales of domestic products and buy or exchange goods from and other countries. It is a necessary trade means between the different countries. The country can export the goods which have their own countries' advantage, and import the goods from other countries that they do not have the production advantages, thus to achieve a equal supply and demand relationship

When a country's currency appreciate, this currency's position will be changed in the world market at same time. If one currency exchange rate has benn changed against with other countries' currency, directly affects the trend of import and export trade between the two countries. then the export and import trade trends would be changed between the two countries, which making a direct change in the value of imports and exports between the two countries.

When the currency appreciate, if the price of N unit commodity is N before, then the pirce is N+ or N- after the appreciation. Meanwhile, the number of import or export goods quantity is M in the past, corresponding to become M+ or M- now. It can be seen intuitively: the currency appreciation has caused the amount of currency and goods changed in a direct way during the import and export trade. As a price ratio between one currency and another currency, the influence of exchange rate appreciation or

depreciation will be directly transmitted to the import and export of goods'
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service and price, which will affect the size and growth rate of imports and exports. In general, the currency appreciation is conducive to expand import, inhibit the export; and the currency depreciation is conducive to increase exports, decrease imports.

Because there are many factors can affect the volume and price on a countries' import and export trade, for example, the major trade partners' economic outlook, market demand and supply, financial and price situation, the national trade and investment policies(such as export tax rebates, interest rates, quota and license management, etc.)changes, and other supply or demand elasticity factors, therefore, short-term fluctuations of the exchange rate's impact on exports and imports are usually not large. But if the exchange rate has changed to one direction in a long period, hen the impact on the export and import growth will be significantly demonstrated.

The exchange rate are free floating in many countries. However, the most mature economies are offer try to maintain their exchange rate stablely. If the exchange rate fluctuate too much, then it is difficult to control the costs in the transaction for importers and exporters, which is not good for import and export trade.

In the past 20 years, China's RMB exchange rate have had a few adjustments, but has maintained stable generally, which has provided a good condition for the import and export's steady growth. In 1994, the first exchange rate reform has made RMB exchange rate back to a reasonable level. Since then, the government has implement a managed floating policy for RMB exchange rate, and floating direction is upward basically. In the

middle of 1995, the RMB against the U. S. dollar has appreciated nearly 4. 5 percentage, and China's imports and exports trade has grew rapidly during these period, exports began to appear large surplus. After the Asian financial crisis 1997, because the Chinese government promised RMB would not depreciate, the RMB has appreciated at least 15% against a basket of currencies. By the influence of financial crisis and the real exchange rate appreciation, China's export growth rate has decreased a lot, and trade surplus reduce at the same period. Since then, the RMB began to lock on U. S dollar for a long term. After 2002, China's imports and exports began to grow again. Throughout these 20 years, we can find that whenever there was a substantial change in the exchange rate, import and export growth rate will appear a significant growth or slow down in this period. However, China's import and export has grew rapidly, especially in the last six years, and the growth are mainly depend on some factors such as the internal and external market's demand and supply, industrial transfer and progress, the competitiveness promotion and foreign trade policy and institutional. Some Chinese and other countries' scholars have used several mathematical models to analysis the influence of RMB appreciation on China's import and export of, although they obtained different data results, but most think that there is a certain relevance between RMB real exchange rate fluctuations and import and export trade. When the appreciation and depreciation rate is lower than 5%, the impact of the exchange rate on exports and imports is not significant. But appreciation or depreciation arte of RMB is large, the effect will be large relatively. Impact range is generally 1: 0. 5-0. 8.[1] In other words, the RMB reevaluate 10 percent, export growth rate should slow

down 5-8 percent by this appreciation effect, and imports growth rate should speed up 5-8 percentage points in general.

According to the experience of several changes in the nominal exchange rate and real exchange in the past years in china, and consider the effects of supply and demand's elasticity is very low for China's import and export commodities, a greater proportion of processing trade, the obvious advantage of industry concentration degree, the level of productivity and management continued to improve, the export advantage product still have much price space to negotiate and other factors, the write estimates the actual impact of RMB appreciation levels (factor) on export and import might be lower, should be in the range 1: 0.3-0.4, which means if RMB appreciate every 10 percent, and export growth rate will be slow down by 3-4 percentage points by this effect, the growth rate of imports in should speed up 3-4% in general.

Chapter 2 The influence of RMB Appreciation on China's Import and Export Growth

The influence of exchange rate movements on export trade is mainly through the price adjustment mechanism conduction, but there are the many factors can effect this mechanism transmission. In china, the processing trade is always after imports raw material and machinery equipment, which produced in China again and then re-export, therefore, there is a large proportion of import raw materials in the processing trade, and this is also because the current stage of economic development caused in china. But with the upgrading of industrial structure in China and the rapid development of basic industries, the needs of raw materials in export

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products, components and semi-finished products will be produced by more Chinese domestic manufacturers, and the adjustment of the exchange rate will also have some expansion effect on the export trade. The impact of currency appreciation on exports are: When the production of export goods are produced by their own country's raw materials and the situation of the currency is devaluating in domestic country, the currency exchange rate appreciation would significantly increase the price of export commodities, resulting in reduced export; if the value of currency is stable in domestic country, the currency appreciation would lead to increasing the price of the foreign currency of export commodities, resulting in reduced the amount of the exports goods; but if the value of domestic currency appreciate, whether the export price of foreign currency rise or not, and the scope size of rise are caused by both of the rate of domestic currency appreciation which make the local price of exports goods decrease, and the range of rising of foreign currency import prices as the appreciation domestic currency,. If the former is larger than the latter, then the exports will increase; if the former is equal to the latter, then there is no affect on export; if the former is lower than the latter, the amount of export good will be reduced. However, When the raw materials of production come from overseas, the relationship between the impact of currency appreciation on exports and the proportion of imports raw materials in export production is inversely, if the proportion is large, then the effect of reducing export caused by exchange rate appreciation will be small, vice versa.

Since China's exchange rate mechanism has reformed on 21 July 2005, the exchange rate of RMB has appreciated cumulatively 11.4% to U. S. dollar, 8.

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2% to the euro, 9.7% against the Japanese Yen, and appreciated 11.5% to the Hong Kong dollar until 15 November 2007. If according to the weighted average of the amount of China's foreign trade, then the appreciation of weighted RMB exchange rate is probably 6.1%, and the annual appreciation rate is less than 3%.

So far, under the situation which RMB has not appreciated too much, there is no big fluctuation for China's import and export. The author has collected the quarter of import and export data from 2005 to 2007, (see table below). In 2006, China's total exports grew 27.2% than the previous year, and the rate of growth has dropped 1.2% against 2005; the amount of import grew 20.0%, and rate of growth increased 2.4 than previous year, respectively. From January to October in 2007, China's export grew 26.5%, almost the same as last year; and the imports grew 19.8% which dropped 1.1% compared to the same period last year. The main reason of recession of export speed-up against the previous two years is that the Chinese government has increased the resource tax for the part of resources export commodities, adjusted tax reimbursement for export and policy of processing trade, as both of the Chinese domestic investment demand and the prices of resource import's products has improved, so there was a slight increase in the import growth rate.

Quarterly growth of import and export since RMB appreciation

Unit: 100 million U. S. dollars

Month

Export

Import

Amount

Compared to the same period last year

Amount

Compared to the same period last year

Third Quarter 2007

2040. 5

29. 1

1753. 1

19. 6

Fourth Quarter 2007

2156. 4

21. 7

1821. 2

22. 2

First Quarter 2008

1972. 7

26. 6

1739. 4

24. 8

Second Quarter 2008

2313. 5

24. 1

1933. 9

18. 4

Third Quarter 2008

2627. 5

28. 8

2140. 2

22. 1

Fourth Quarter 2008

2780. 8

29. 0

2103. 3

15. 5

First Quarter 2009

2520. 1

27. 7

2056. 4

18. 2

Second Quarter 2009

2946. 6

27. 4

2285. 6

18. 2

Third Quarter 2009

3315. 6

26. 2

2583. 4

20. 7

Fourth Quarter 2009

3612. 3

29. 2

2681. 7

27. 5

Data source: Customs statistics

According to the different country's which do international trade with china, except the growth rate of export to Japan has been sluggish in recent years, the exports trade from China to European Union United States, Hong Kong and other staple market grows strongly, and imports trade grows steady.

According to the customs statistics from January to September in 2009, the export growth rate from China to EU and ASEAN grows fast which is more than 30% in the top 5 largest trading partners, and is 10%, 15% and 20% higher than to Hong Kong, the United States and Japan, respectively, In addition to strong economic growth in the EU and the ASEAN, it is also because RMB appreciated not too much against the EURO, obviously.

Meanwhile, there is no big difference of imports growth rate for the countries which import production from china these years, shows that the impact for import of these countries from china is limited caused by RMB appreciation.

Overall, if we can take out other factors, the influence of small RMB appreciation on the import and export can be ignored.

From January to September 2009, the trade between China and other main countries

Unit: 100 million U. S. dollars

National or Regional

Export

Growth^{1/4}%^{1/4}%

Import

Growth^{1/4}%^{1/4}%

European Union

1755. 2

30. 8

806. 2

21. 7

United States

1699. 9

15. 8

513. 7

15. 1

Japan

739. 8

11. 1

979. 6

16. 3

ASEAN

674. 8

31. 7

790. 5

21. 5

Hong Kong, China

1322. 2

21. 6

92. 3

15. 6

Data source: Customs statistics

According to the report from import and export enterprises, although they may feel some pressure from small appreciation of RMB, but generally the customer would consider a certain of RMB appreciation factors when they

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sign for the export contracts. They still concerned more about market trends and export tax rebates, and other policy changes. However, the import enterprises feel that there is not too much stimulation for imports on the small RMB appreciation, which is so small influence compared to the change of real price of imported goods.

If the RMB exchange rate continued to appreciate slowly, the total impact on China's export and import growth will be still limited. First of all, the world economy continues to grow steadily, the investment and consumption are still hot in China, both of the domestic demand and external demand of china are quite strong which influence Chinese economy much more than the changes of RMB exchange rate; Secondly, the processing occupies nearly half proportion of Import and Export, and this part of imports and exports does not effected by the exchange rate changes; Third, enterprise and market has prepared to take the pressure from RMB appreciation; Fourth, the improve of industrial technology and labor productivity could be offset some influence on the RMB appreciation, making the export cost do not rise quickly; Fifth, China has the comprehensive competitiveness which could make the processing export industry can not be replaced easily by other countries in the short period, and making china also has the pricing power in some kind s of the export products.

Under some market pressures, if exchange rate of RMB against the U. S. dollar appreciate more than 10% in the end of 2010, and trade-weighted exchange rate increased over 15% at the same time, then there will be a significant impact on china's exports and imports, and it will be difficult for

Chinese company to export some low value-added goods or some exports
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products which depend on low-cost competition, but the competitiveness of imported goods would be increased. In this regard, every import and export company concern about exchange rate. According to the data(coefficient) of change of RMB exchange rate which has been calculated above, the growth rate of import may be 3% to 5% higher than in 2008 and 2009, but the growth rate of exports may be 4% to 6% lower than in 2008 and 2009. Foreign trade on GDP growth, and the pulling effect of foreign trade on GDP growth from will be under a certain influence, but this effect will be still under an affordable range. Unless the major turmoil or crisis occurs again, or there will not appear the situation which the amount of export decrease sharply like in 1998's Asian financial crisis .

In the long run, through the transmission and regulation of prices, RMB appreciation will cause different influence on the growth rate of import and export, commodity structure, trade patterns and the trade-related investment in China.

2. 1 The beneficial effect of of RMB appreciation on foreign trade growth

Firstly, The RMB appreciation can improve the trade conditions. With the trade surplus increase rapidly, China's terms of trade are deteriorating in recent years. A survey report from Commerce Department shows that from 1998 to 2008 the overall terms of trade index of china has decreased by 13% as the 2003 is base period. Which terms of trade of manufacture fell by 14%, primary products decreased by 2%. The export price index and imported goods price index are 104. 7 , 109. 7 in 2008, respectively. Terms of trade index is 95. 4% in 2008 which is lower than 98. 8% in 2007. This

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means that the rate of China's export prices of import prices is falling, so china must export more goods as to exchange for the same amount of imported goods, and loss national welfare during the foreign trade. In recent years, Chinese government leads the investment in fixed assets always staying at a high level. The proportion of Imported energy and raw materials, primary products, high-tech chemical products, machinery and transport equipment, manufactured goods increased sharply. Recent years, the unit dollar price of most of the primary products, capital, and technology-intensive products have increased a lot. From 1998 to 2008, the import price index rose by 19%, which manufactures increased by 20%, primary products increased by 16% in China. Meanwhile, the rapid development of Chinese economy has led import demand increase fast, and caused the price of international material and technology-intensive products rise, further caused the term of trade worse.

RMB appreciation will lower prices of imported goods, especially lower the price of raw materials and high-tech equipment, then companies will introduce the technology faster, improve production efficiency, carry on more product replacement and achieve products upgrade quicker than before. At the same time, because most imports will used to be re-exported, and with the improve of enterprise productivity and export product quality, it is helpful for extending the Chinese enterprises from low-end products chain to high-end chain, improving the terms of trade simultaneously. This will help china's enterprise using world resource better and increase the national welfare. Overall, it will enhance the international competitiveness of Chinese products.

Secondly, the RMB appreciation can optimize the commodity structure of foreign trade. At present, China's trade structure is very irrational, most of enterprises are labor-intensive and with low technology, the only part of high-tech and deep processed export products are still have some short processing and low value-added problems, and real high-tech equipment and intermediate inputs are still imported from other countries, and nearly 80% of profit not belong to the china's re-produced enterprise. However, The RMB appreciation would reduce the cost of enterprise's independent development, promote the technological upgrading indirectly, enhance their core competitiveness, thus accelerate the pace of industrial upgrading, promote export structure adjustment.

Thirdly, RMB appreciation will increase the wages of worker, which will make it easier for attracting high-tech employee. under the independent innovation and technological promotion in China, the foreign entrepreneur will choose to invest high tech industry first, so that China's industrial structure and export commodity structure will be optimized. The next point is that the RMB appreciation will help Chinese enterprises for promoting the oversea investment. As the enterprise must use the local currency so that they can invest in other countries, so RMB appreciation reduces the cost of oversea investment significantly, and enhance the enterprise's international purchasing power and foreign investment capacity, create the condition for those enterprises who wants to develop their business.

Finally, RMB appreciation will make service industry and service trade develop better, then the low value-added, poor management, and low efficiency enterprise would be kicked out effectively. It also change the <https://assignbuster.com/rmb-appreciation-on-chinas-import-and-export-economics-essay/>

situation which industry (mainly the second industry) aggregate most of the resources, , thus contributing to change China's industrial structure to service industry easily and promote service industry develop rapidly, then make coordinated development of service trade and merchandise trade come to ture, and improve the competitiveness of whole country in the end.

2. 2 The adverse effects of of RMB appreciation on foreign trade growth

RMB appreciation, it means the amount of Yuan exchanged form U. S. dollar will be less and less, then for the exporter, it is the same theory that the amount of Yuan exchanged from one U. S. dollar goods is less than before because of RMB appreciation. Therefore, there will be a certaion influence on the profits of exporter. If from importers' angle, the amount of Yuan to purchase one U. S. dollar goods is decreasing, so the cost of imports drop, and profits rise. However, because industry and cost structure are different, we need to distinguish the adverse impacts of RMB appreciation on different export enterprises. The growth of resource commodities, part of the staple agricultural products and low value-added manufactured exports slow down or even fall, there would be some adverse effects on the income for export agricultural farmers and part of low-skilled workers. Some large-scale complete sets of equipment needs 5-10 years from contract to delivery, and the payment time may be longer. If the RMB maintain appreciation trend in a long-term, it is difficult for enterprise to predict the long-term exchange rate, however the financial institution only provide foreign exchange hedging instrument in one year generally, so the enterprise has to undertake more exchange rate risks and avoid risks.

There is a fundamental negative impact of RMB appreciation on textile export. Textile products have been the number one of China's exports for a long time. Until 2005, textile trade surplus is still higher than the entire foreign trade surplus. The textile industry has always been the backbone of china's export trade, industry export dependence up to 50%. However, most of the textile exports are based on low labor cost and price advantage, the profit margins is not high. According to the calculations from China's first textile website, if RMB appreciate 1%, the then the amount of textile industry sales would fall 2% to 6%. From January to October 2006, the overall profit margin of China's textile exports is 3.9%, if the speculation was right, then 5% of appreciation of RMB, and the textile industry profit margins will drop 10% at least. Therefore, if RMB appreciate more than 10%, it will cause an obviously impact on textile industry. However, some low-tech enterprises will quit this industry under this low profit export situation, forcing the textile companies to enhance the added value of products, construct brand concept, improve their core competitiveness. In the long run, in order to improve China's textile industry's competitiveness in the international market, Chinese government must catching this good opportunity of good economy development trend in china, using the large amount of international surplus, and start the structural adjustment in the textile industry.

The growth of most raw material products export will be slowed. The majority of china's raw materials export products have less competitive in price, and has strong dependence on the exchange rate. For example, paper, cotton, ferrous metal(steel, crude steel, manganese, etc.), aluminum, lignin

ornament and so on. RMB appreciation will make these primary products, raw materials products export's growth to slow down, also have a negative impact on economic growth in the short-term. RMB appreciation will also reduce the amount of export of crude oil, refined oil, timber, copper, gold and other resource-based goods, then it will cause the rate of unemployment and the banks' bad debts increase, and other related effect. [5] Because china do not have too much resource which normally used in high energy and high-polluting industries. The excessive export of resource products will increase intense contradictions in using coal and gas in a short time. It will increase the pressure of environment and resource, which is not good for the sustainable development of economy in the long-term.

The electrical appliance industry will suffer lots of loss for export. China's electrical appliances has the Comparative advantage due to the relatively low-cost, so that China has become an important production base for the home appliances giants. Sales of appliances industry is mainly depend on the international market, and export has become a major demand source for household appliances industry. The RMB appreciation a tremendous negative impact on the electrical appliances product's export, cause its low profit margins drops further.

If the exchange rate of the Yuan appreciate rapidly, then the impact on export and import growth may not be so mild. First, the export growth rate may result in significant downturn, then there will be big shock not only for the resource, low price and the low value-added goods, but also for the whole export processing industry. Secon, it possible to stimulates the large

quantities of goods imported, impact the china's domestic markets and cause a certain deflation.

Finally, it will be the psychological effect on people from the impact of trade. The production cost will transfer to the price on the international market, so the exchange rate appreciation will not affect too much for this kind of products' profits. The appreciation of the RMB increase the international enterprise's cost in china, but these enterprises have relative cost advantage in the international market, which has the minimal impact on the international trader's profit. However, the normal people will think that the price of "made in china" has increased a lot as the appreciation of RMB, and the business people will think that they could not earn much money from china imported products, thus it will cause real adverse effects for Chinese exports.

Chapter 3 The marco countermeasure of RMB Appreciation on Import and Export

3. 1 The adjustment of marco financial policy about RMB appreciation

Firstly, Chinese government should expand the government expenditure and promote pull effect of china's domestic demand on economic development.

In recent years, due to the investment scale on iron and steel, electrolytic aluminum, cement, real estate has grew fast, and has caused the price of upstream products and raw materials rose too high, for instance, the price of electricity, oil and transportation has became extremely high. Although the investment is better than the consume for economic growth, but in the composition of china's domestic demand that investment must be under

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control. Therefore, the stimulating domestic demand policy should be focus on consumption. But the income gap between the rich people and poor people in china which make many people can not afford some consumption even they want to consume. Since that it is difficult for the common people to consume more in short run, therefore, the important task of expanding domestic demand should be taken by Government. Since a long time, why the China's consumption is always weak, not only because government consumption expenditure is not high, but also because social security system does not work very well for the consumers. Therefore, china must reform their public finance expenditure patterns, under the situation which the whole social investment is overheat, the financial expenditure should be changed from investment to consumption, and the financial expenditure should withdraw from the competitive field of investment as soon as possible, then put more financial resource on the public goods. Therefore, the writer think the public expenditure should be invested in the following key areas: First, the manufacturing industry which can support development of the economy for a long time; Second, increase the government financial expenditure on health system, old-age pension and social security welfare, in order to reduce the people's long-term financial budget and saving, then they can expand their consumption; Third, the government should decrease the farmers' burdens and handle the problem of " agriculture, farmer and rural area" well.

Secondly, china must adjust the consumption tax, reduce the export tax rebate rate and the trade surplus. At present, China is still in economic transition, there is still a large gap between china and other developed

countries, and social security level is still very low. Meanwhile, because the economic opening time is short which is only more than 30 years, the influence of traditional culture on enterprise and consumer is still large, and the relationship between investment and consumption is quite conservative, an