

Renminbi our  
currency, is it your  
problem



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China's Renminbi: "Our currency, Your Problem"? China in the last century has gone through many dramatic changes. 35 years ago there would not even be talk about China's currency because under Mao ZeDeng all trading with China had to be through the British colony of Hong Kong. Now China has opened up its economy and allowed many companies to privatize. The problem facing China and U. S. relations revolve mostly around two main elements; trade deficit, and currency.

The most important cultural aspect which must always be in the back of one's mind is that China is still under a communist rule, meaning that the government has more control of businesses and industries than many of the countries which the US handles trades. At the moment, the American government has made it clear that it has concerns about the Chinese government interfering with its currency, specifically undervaluation the ??? . Under a new law that was passed in 2011, if a country's currency is determined to be a "currency manipulator" then the Obama administration can take legal action against China. Chinese officials... threatened a trade war"[1] when they learned that the United States Congress was trying to pass this bill. This is a small example of the tensions between the US and China because of currency. If there were to be a revaluation of the Yuan, which would lead to an appreciation of the currency there will be major effects in China's business. China is a country where 33% of its GDP (2012) is manufacturing, the highest in the world. [2] Most of their manufacturing comes from foreign companies who move their plants to China to produce goods at a lower cost.

This lower cost comes from the exchange rate between these Western countries and China, which favor the developed countries. With China's currency stronger, these developed countries get less money for their currency, thus making goods more expensive. Consequently on the other side, goods produced outside China, like in Germany or the United States would be less expensive than before the revaluation. With the cost of manufacturing increasing, China may lose business with all these foreign companies whose reason for moving manufacturing in China was lower costs.

Another problem that China will face with an appreciated Yuan is the effect it will have on the Chinese US treasury bonds. Along with the huge trade deficit, China holds a lot of US treasury bonds, because when China's market was first opened up, many of the Chinese believed America to always be stable. With the low interest rate and the appreciation of the Yuan, China will not be making as much, if any, off of the bonds. Once more and more Chinese begin to figure that out, less will buy US treasury Bonds.

Since China owns a majority of US debt, if China stops buying debt from the US then the US will lose a huge intake of cash flow. [3] With a revaluation of the Yuan, many goods that are made in China will increase in price. This will cause some companies that produce low-cost products, to move their manufacturing to countries that are cheaper to do business with. Meanwhile, with a growing middle class in China, more will be able to afford goods that for example, are made in America, thus, exporting to China will be cheaper.

This change in trading may help with the US and China trade deficit; even though there will still be a deficit because of the bonds China holds, it will be

more balanced than before. With regards to imports and exports in China, a revaluation should cause the goods from Western countries to be cheaper in China; however, China has a double taxation on luxury items. For brands like Nike, they will not be more expensive, but for brands like Ralph Lauren, Cartier, Chanel, their products will be even more expensive because the Chinese government will tax them again more heavily, in order to try to promote their own luxury brands.

Since most of these Western countries produce high luxury goods, this is not good news. With a raising upper and middle class, there are more Chinese who can afford these goods, but because of the governments' double taxation, they are still making these products unaffordable. [4] Japan's relationships with the western countries will increase if there is a revaluation of the Yuan, but it will hinder the relationship between China and Japan. Japan also manufactures some of its products in China so that it can also produce products at a lower cost.

Also, many companies have manufacturing in Japan because it is easier to ship products from China and finish the final product in Japan because it is geographically closer, and therefore cheaper. Japan has also been running a deficit with China since 1995, and China became the number one trading partner in Japan. An appreciation of the Yuan will make goods in Japan more expensive. [5] However, without regards to the appreciating Yuan the new President in China, Xi Jinping, Japan and China relations are to be forecasted to become stronger. For some countries, an appreciation of the Yuan is beneficial.

For NIE's and developing countries, they are now beginning to look favorable to western companies that wish to produce goods at a cheaper cost. Countries like Vietnam, Indonesia, and Bangladesh will look favorable because manufacturing in these countries will be cheap and their currencies are more favorable to western countries. For workers in China an appreciation in Yuan will be good for the migrant workers who flock to the coastal cities to work at these lower paying jobs. Their money is now worth more and will allow them to buy more products that are not made in China.

With an appreciation, more manufacturing will be leaving china, and therefore taking jobs away from China, so an appreciation is a double edged sword for the workers of China. Generally speaking, exports for manufacturing goods will be lower, and China may start importing from other countries for low cost goods. Imports for goods made in Western countries will increase. Since China has been working on their IT industry, China does have a saving grace. Lenovo is now the number one computer manufacturer in the world. Many businesses in Asia are buying more and more of Chinas software and information technology.

The exports for It will increase. All of these assumptions are only taking into consideration for the appreciation of the Yuan. There are other factors that go into cheap manufacturing like purchasing power parity, cost of labor and supply chain. Many other supporting industry companies have gone to China to make it easier to produce goods. If manufacturing were to move to other countries, these other industries and companies would also have to move. There is one other element that is important to consider, that the Yuan is not as undervalued as the US government claims.

After joining the WTO, China had to agree to completely give up control of the banks by the end of December 11th 2011. With this bank reform, China has less control over manipulating their currency. According to Eswar Prasad at Cornell University, the IMF will have a difficult time creating a strong case the Yuan is undervalued. " All of the relevant indicators, the currency account and trade surpluses, the pace of reserve accumulation and the exchange rate itself have moved in the direction of suggestion the Yuan is no longer much undervalued,". 6] There is no doubt that the Yuan is going to continue to appreciate, however it is becoming more and more apparent that the currency is not being as manipulated as it was before. -----

[1] Favole, Jared A. , and Ian Talley. " Obama Urges Caution on RMB Bill. " Wall Street Journal [New York] 7-8 Oct. 2011, World Business sec. : 6. Print.

[2] " Investing and Economics Blog. " Manufacturing Output as a Percent of GDP by Country at Curious Cat. Curious Cat, n. d. Web. 07 Feb. 2013. [3]

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