

# FINANCIAL TIMES

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## China currency is 'no longer undervalued', says IMF

By Tom Mitchell in Beijing and Shawn Donnan in Washington

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The International Monetary Fund has declared that China's currency is "no longer undervalued", marking a significant shift after more than a decade of criticism of Beijing's tight management of the renminbi.

The move amounts to a major vote of confidence in Beijing and the renminbi at a critical time. It also puts the IMF at odds with its biggest shareholder, the US, which insists that

China continues to draw an unfair trade advantage from a renminbi that it considers "significantly undervalued".

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The renminbi has gained 25 per cent against the US dollar since it was allowed to adjust upwards within a narrow band a decade ago, and has held its value even as the dollar has strengthened against other major currencies over the past year.

But many economists — and, until Tuesday, the IMF fell into that camp — have long considered the renminbi to be undervalued. They have pointed to Beijing's historical tight control of the currency's value as a major factor in the rise of China's export-oriented economy to a point where it is now the world's leading trading nation.

Speaking in Beijing at the end of a regular review of China's economy, David Lipton, the IMF's first deputy managing director, said: "While undervaluation of the renminbi was a major factor causing large imbalances in the past, our assessment is that the substantial real effective appreciation over the past year has brought the exchange rate to a level that is no longer undervalued."

In Washington a senior US official said that while the US welcomed the recent appreciation in

China's currency it remained of the view that the renminbi was "significantly undervalued" with China's trade surplus with the US and other nations strong evidence of that.

Eswar Prasad, the former head of the IMF's China unit, said the shift by the fund was important as it marked the first time since the Asian financial crisis of the late 1990s that the fund had not deemed the renminbi to be undervalued. It also presaged the likely adoption later this year of the renminbi as one of the small number of major currencies in a basket used to determine the value of the IMF's de-facto currency, the Special Drawing Rights.

China has publicly expressed its desire for the renminbi to join the dollar, yen, euro and sterling in the SDR basket — a move that would see it recognised as an official reserve currency.

"We welcome and share this objective and will work closely with the Chinese authorities in this regard," Mr Lipton said on Tuesday, noting that the IMF's stated position on the renminbi's inclusion in the SDR "is not a matter of 'if' but when".

The IMF is conducting a review of the SDR facility and its constituent currencies that is due to be completed later this year. To be included, the renminbi must be deemed to be "freely usable".

The new appraisal by the IMF "paves the ground for an assessment that the currency's value is largely market-determined", Mr Prasad said, thus removing one potential argument against the renminbi's inclusion.

"In co-operation with the Chinese government, the IMF appears to be gradually and methodically putting in place the building blocks necessary to strengthen the case for the renminbi to become part of the SDR basket," he said.

The US has withheld judgment on whether the renminbi should be included in the basket. The US official said plans to add the renminbi would be discussed at this week's G7 finance ministers' meeting in Germany.

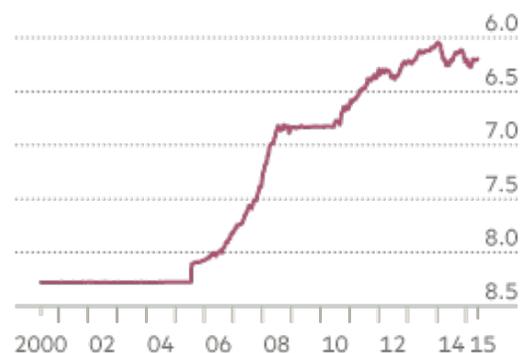
Tuesday's pronouncement on the Chinese currency came as the IMF urged Beijing to continue with difficult financial reforms even if growth slows to as low as 6 per cent.

Noting that the stimulus-driven expansion of China's economy in the wake of the global financial crisis had "relied on a mix of credit and investment that we felt couldn't and shouldn't be sustained", Mr Lipton called on Beijing to "continue to address vulnerabilities even if that requires allowing growth to slow into the range of 6 to 6.5 per cent".

The IMF has predicted previously that China's economy would grow 6.8 per cent this year — below

### Chinese renminbi

Against the dollar (Rmb per \$)



Source: Thomson Reuters Datastream

FT

the government target of about 7 per cent — and just 6.25 per cent in 2016.

The IMF was critical of other aspects of China's reforms, including the slow transformation of the country's state-owned enterprises (SOEs).

“Levelling the playing field between the private and public sectors is a key goal of the [reforms],” Mr Lipton said, adding progress on this had been “too slow”.

The IMF also called on Beijing to increase SOE dividend payments to their government owners, eliminate subsidies and allow state-sector bankruptcies.

Beijing has directed state banks not to stop lending to insolvent infrastructure projects backed by local government finance vehicles, which borrowed vast amounts of money to prop up growth during the global financial crisis.

Local governments are saddled with an estimated Rmb22tn (\$3.54tn) in debts, while China's overall indebtedness has almost doubled to 250 per cent of GDP since 2008.

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