U.S.-China currency deal won't change dollar-yuan dynamics: experts

WASHINGTON (Reuters) - A U.S.-China currency agreement being floated as a symbol of progress in this week's trade talks between the world's two largest economies would largely repeat past pledges by China, currency experts say, and will not change the dollar-yuan relationship that has been a thorn in the side of President Donald Trump.

FILE PHOTO: U.S. 100 dollar banknotes and Chinese 100 yuan banknotes are seen in this picture illustration in Beijing, China, January 21, 2016. REUTERS/Jason Lee/Illustration/File Photo

Such a deal would, however, provide the U.S. Treasury an opportunity to climb down from what currency experts say was a misguided declaration in August that Beijing was a "currency manipulator," reducing the yuan's value to gain "unfair competitive advantage in international trade."

Little is known about the structure of a currency deal that the U.S. Chamber of Commerce said American and Chinese negotiators were working toward on Thursday in their first high-level trade talks since July, but it is widely expected to include a promise from both to sides to refrain from devaluing their currencies to gain a competitive trade advantage.

As members of the Group of 20 major economies, both the United States and China agreed to such language starting in 2010.

At that time, China was widely seen to be deliberately holding down the value of its heavily managed currency, also known as the renminbi (RMB). But this intervention shifted to mainly prop up the yuan's value after a sharp devaluation in 2015.

It is unclear how a pact with the United States might change Beijing's behavior.

"In essence, I don't see anything in a currency deal that will cause a significant change in the present RMB/dollar currency market dynamics," said Mark Sobel, a longtime former Treasury and International Monetary Fund official who is now U.S. chairman of the Official Monetary and Financial Institutions Forum, a London-based think tank.

Myron Brilliant, head of international affairs at the U.S. Chamber of Commerce, said a currency deal would likely be accompanied by the United States' canceling a planned tariff increase to 30% from 25% on $250 billion in Chinese imports.

A U.S. official confirmed that currency would likely be discussed in the talks, but it was premature to say whether an announcement would be made on the issue this week. Optimism over the talks had improved after the first day's negotiations wrapped up.

U.S. Treasury Secretary Steven Mnuchin, a principal negotiator in the talks along with U.S. Trade Representative Robert Lighthizer, said as early as February that Chinese Vice Premier Liu He had largely agreed to currency language. But talks on a broader deal to end the trade war between the United States and China broke down in May, leaving the currency provisions in limbo.

YUAN STABILITY

Mnuchin has long pushed his Chinese counterparts for increased transparency in yuan market interventions by China's central bank and to maintain a stable yuan value against the dollar.

In August, after the yuan fell below the psychologically important level of 7 to the dollar in response to a new round of U.S. tariffs, the Treasury Department declared China a currency manipulator for the first time in 25 years following Trump's own tweets that China was manipulating the yuan.

The designation under a 1988 law requires the Treasury to enter into negotiations with the offending country to correct the situation — an effort that had been under way for more than two years.

The International Monetary Fund disagreed with the designation, arguing that the yuan's value was in line with China's trade-battered fundamentals. Beijing had actually been spending reserves to prop up the yuan's value, not push it down to make exports cheaper.

Eswar Prasad, former head of the IMF's China department and now a trade professor at Cornell University, said it would be convenient time for both sides to agree on the need for maintaining a stable dollar/yuan value — even though this goes against longstanding U.S. demands that China allow its currency to float freely.

If so, the United States would get an assurance that yuan devaluation would not undermine its tariffs, while China would reduce the risk of capital outflows from perceptions that it is trying to weaken the yuan, he said.

"This issue could give both sides cover to strike a mini deal that has little substance but de-escalates tensions at least temporarily, which could stabilize market sentiment and have some positive effects on both economies," Prasad said.

CURRENCY REPORT

An agreement could also allow the Treasury to declare that its manipulator designation on Beijing had been resolved. The Treasury will need to address the designation in its semi-annual currency report, due on Tuesday.

Mnuchin has said that currency provisions in the new U.S.-Mexico Canada Agreement represent a model for future trade deals, although these were not repeated in a newly signed limited trade deal with Japan.

The USMCA language closely tracks the G20 language. The North American trade deal, which still needs ratification by the U.S. Congress, requires the three countries to disclose monthly data on international reserve balances and intervention in foreign exchange markets, along with quarterly balance-of-payments data and other public reporting to the IMF.

“If China publishes intervention data and is more transparent about its currency practices, that’s a positive,” said Sobel of the Official Monetary and Financial Institutions Forum, although he noted that China already publishes reserves data, which show that it has not intervened to prevent the yuan from rising for years.

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