China Pressured to Let Yuan Rise

U.S. Fed chief’s call for change in currency policy comes as IMF report says revaluing wouldn’t crimp growth

By BOB DAVIS

WASHINGTON—China came under more pressure to let its currency rise as Federal Reserve Chairman Ben Bernanke said flatly that the yuan is “undervalued…to promote a more export-oriented economy” and an International Monetary Fund study suggested that a currency move wouldn’t harm Chinese growth if handled properly.

Mr. Bernanke, making his strongest comments on the subject in speaking before Congress’s Joint Economic Committee, said, “It would be good for the Chinese to allow more flexibility in their exchange rate” to “address inflation and bubbles within their own economy” and to help bring more balance to a global economy in which China relies too much on exports and the U.S. too much on borrowing to import.

But Mr. Bernanke, responding to questions from China critic Sen. Chuck Schumer (D., N.Y.) also said that moving the exchange rate alone wouldn’t have a major short-term effect on trade flows—though “over time it would have an impact.”

The Fed chairman’s remarks come amid growing expectations that China will allow its currency to rise, perhaps before leaders of the Group of 20 industrialized and developing countries meet in Canada in June.

The U.S. Treasury recent postponed a decision on whether to label China a "currency manipulator," an apparent effort to give China some political breathing space to revalue its currency without appearing to bow to U.S. pressure.

The focus on the yuan comes as the Chinese have balked at fully participating in a process organized by the G-20 to better coordinate economic policies across countries, says Eswar Prasad, a former IMF senior official for China. He said China has viewed the effort as a lightly veiled attempt to pressure them on the yuan.

Each country is supposed to submit proposed policies to the IMF, which then is to judge whether the plans, in total, would produce sustainable growth.

G-20 countries aim to use the analysis to press one another to make changes.

Several government officials say the so-called mutual assessment process got off to a rocky start after China supplied only a single year’s worth of data, rather than the five years’ worth that China Pressured to Let Yuan Rise - WSJ.com
the IMF sought.

After a G-20 planning session in Korea in February, several officials said, China made efforts to meet IMF data requests, although a number of G-20 officials remain skeptical of Beijing’s intentions. “The [Chinese] government does not traditionally make medium-term projections,” sought by the IMF, said China’s IMF representative He Jianxiong. “However it has come up with data just for this exercise.”

In their World Economic Outlook, IMF economists analyzed 28 instances over the past half-century when countries cut their trade surpluses. On average, the surplus narrowed by 5.1 percentage points of gross domestic product in the cases studied, but the countries’ growth rate didn’t change appreciably.

Any economic decline caused by an appreciation in currency was offset by other policies, including government stimulus aimed at boosting domestic demand. “There is no evidence that transitioning out of large external surplus was associated with lower growth,” the IMF reported. Harvard University economist Dani Rodrik, whose work the IMF report frequently cites, said that China’s growth is tied to its exchange rate more than other countries at a similar income level and, thus may not benefit from policy changes suggested by the IMF.

That’s “possibly because China is so huge and with so much labor still in extremely low productivity activities,” Mr. Rodrik said. The lesson for China shouldn’t be “full speed ahead,” Mr. Rodrik said, but rather, “caution is warranted.”

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