

Obama sets stage for likely trade war with China



by P. Parameswaran

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WASHINGTON (AFP) – US President Barack Obama has set the stage for a possible trade war with China by branding the Asian giant a currency manipulator, a term his predecessor George W. Bush had skillfully avoided despite pressure from lawmakers.

"President Obama -- backed by the conclusions of a broad range of economists -- believes that China is manipulating its currency," his Treasury secretary-designate Timothy Geithner said Thursday in written testimony to senators quizzing him over his pending confirmation.

Obama, who took office only Tuesday, has pledged to "use aggressively all the diplomatic avenues open to him to seek change in China's currency practices," Geithner said.

Under the Bush administration, the Treasury had stopped short of identifying China a currency manipulator in its semiannual global currency reviews, acknowledging however that the yuan was relatively undervalued against the US dollar.

By directly branding China, Obama has laid the groundwork for trade friction between the key powers, both reeling from global financial turmoil that has slammed the brakes on growth and triggered a host of domestic problems.

"This is definitely setting the stage for some bad blood between the two countries and I anticipate that over the next year or so, trade fiction is going to become somewhat more heated," said Eswar Prasad, former China division head at the International Monetary Fund.

He said Obama's charges came as China used its competitively priced exports to fuel growth and check rising unemployment, disregarding international advice that it wean away from exports by using domestic consumption as a linchpin for economic expansion.

"It signals a much harder line I think the Obama administration is going to take in public," Prasad said, contrasting the new administration's policy with the Bush administration's strategy of prodding Beijing in private to allow the yuan to appreciate.

As an Illinois senator, Obama had co-sponsored legislation aimed at changing how the US government formally determines currency manipulation and authorizes new trade reprisal measures.

During the presidential campaign, he had accused China of suppressing its currency's true strength to make its exports more competitive, echoing some US lawmakers who blamed the snowballing US trade deficit with China on the weak yuan and have sought sanctions against Beijing.

"If there is a rise in trade tensions, it is much more a reflection of deeper reality rather than anything else,"

said Brad Setser, a former US Treasury official, citing the current economic crisis facing the two powers amid a global trade slump.

"Certainly, it is a signal that the Obama administration is going to put a focus heavily on the Chinese exchange rate regime and make that a key issue in discussions between the US Treasury and the Obama administration and China."

Geithner, who is expected to be confirmed as Treasury chief, hinted that any moves to tighten laws against currency manipulation would ensure that "countries like China cannot continue to get a free pass for undermining fair trade principles."

"The question is how and when to broach the subject in order to do more good than harm," he added.

But heavy US dependence on Chinese capital may limit Obama's options against Beijing.

China has overtaken Japan as America's biggest foreign creditor, and as of October 2008 held 652.9 billion dollars in US Treasury bonds, according to the latest Treasury Department figures.

"To engage in any action that would lead the Chinese to misunderstand actions by the US and therefore sell these holdings would be dangerous," warned Andrew Busch, global forex strategist with BMO Capital Markets.

Busch said that the United States has been reluctant to brand China a currency manipulator for two reasons -- "One, China doesn't meet the Treasury's narrowly defined criteria. Two, China owns a lot of US Treasury, agency and overall debt securities."

US lawmakers had previously proposed legislation aimed at imposing steep tariffs on Chinese products entering the United States if Beijing refused to make its currency flexible.

They also wanted currency manipulation to be classified as an illegal subsidy under US trade law, paving the way for American companies to demand "countervailing duties" on Chinese products.

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Geithner assails China as Treasury confirmation moves closer

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Incoming Treasury secretary Timothy Geithner vowed to get tough with China and redesign the crisis-hit US financial system as his nomination passed a crucial hurdle in the Senate Thursday.

Despite criticism over his personal tax affairs, the Senate's powerful finance committee voted 18-5 to endorse Geithner's appointment to arguably the most crucial job in the new cabinet of President Barack Obama.

While joining fellow Republicans in castigating Geithner's past failure to pay certain US payroll taxes, Republican Olympia Snowe said: "I do believe his resume is essential for this time."

Influential Democrat Kent Conrad said the tax problems arising from Geithner's 2001-2004 employment at the International Monetary Fund were "completely unacceptable."

"In normal times that alone would lead me to oppose his confirmation," he said. "But these are not normal times. I believe we cannot afford further delay in filling this critical position."

Senate Majority Leader Harry Reid has said he will move rapidly to bring the nomination to a vote by the full chamber, as Obama gets to work on tackling the nation's worst economic crisis since the 1930s Great Depression.

The stakes were laid bare Thursday as US stocks swung lower after fresh government data showed weekly jobless claims had shot up to a 26-year high and housing construction starts were on the slide.

Geithner, a senior Treasury official in the 1990s, brings to bear inside knowledge of how the crisis has unfolded from his most recent job as president of the New York Federal Reserve.

At his confirmation hearing Wednesday, he apologized for his "completely unintentional" tax errors, insisting he had paid back 34,000 dollars to the Internal Revenue Service -- which he is now in line to supervise.

Geithner promised a "comprehensive plan" for the economy, starting with the housing market, and vowed to reopen frozen lines of credit by exerting greater pressure on banks that have benefited from a 700-billion-dollar bailout.

Reiterating the cardinal tenet of past administrations, he said "a strong dollar is in America's national interest" as he promised to make wise use of a planned stimulus package worth a whopping 825 billion dollars.

Following up his confirmation hearing, Geithner fleshed out his policy priorities in a 102-page packet of answers to senators' written questions.

On the international front, he wrote that Obama believes China is manipulating its currency, the yuan, and plans aggressive diplomacy to ensure US trading partners play fair.

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"President Obama has pledged as president to use aggressively all the diplomatic avenues open to him to seek change in China's currency practices," he said.

Geithner promised "deep engagement" with China but did not commit to continuing a somewhat fitful "strategic economic dialogue" initiated by the former Treasury secretary, Henry Paulson.

That engagement would cover "currency issues, inadequate intellectual property rights protections, product safety, and non-tariff barriers."

"The yuan is certainly an important piece of that discussion, but given the crisis the immediate focus needs to be on the broader issue of stabilizing domestic demand in China and the US," Geithner stressed.

He pledged to extend the outgoing administration's offensive of banking sanctions "to prevent Iran from misusing the financial system to engage in proliferation and terrorism."

At home, Obama's economic lieutenant said an overhaul of Wall Street was long overdue, promising to look at regulation of unregistered hedge funds and to shed greater light on the opaque role of credit ratings agencies.

"Our financial system architecture is unsound and outdated. We need a fundamental redesign," he wrote.

"Among other things, this includes better prevention and detection methods, better enforcement authority, (a) resolution regime for systemically important non-banks and better checks on excessive risk."

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