

Posted on Fri, Jul. 22, 2005

CURRENCY

China implements new rules for yuan

China announced that it has adopted a new system to value the yuan after pegging it to the U.S. dollar for 10 years.

From Herald Wire Services

BEIJING -- Following months of political pressure, China Thursday revalued the yuan to 8.11 for every dollar, scrapping a decade-long peg to the currency in favor of a more flexible band using a "basket of currencies."

China's announcement, which has been anticipated and debated by economists and government leaders for months, is the first time in a decade that China has raised the value of its currency, also known as the renminbi, effectively making the yuan and exports more expensive against the U.S. dollar.

The move represents China's first step toward the more flexible exchange rate that the United States, Europe and many other countries have called for recently.

Until the announcement, the yuan sold for 8.27 for every dollar.

But the change falls far short of the 10 percent to 15 percent revaluation demanded by many in Washington, where the Bush administration and congressional leaders have been calling for a higher yuan, in part to alleviate America's growing trade deficit with China.

During one of his semi-annual reports to Congress Wednesday, Alan Greenspan, the Federal Reserve chairman, was asked whether the United States should impose tariffs on China to force a currency revaluation. Greenspan responded that such punitive measures would not have their desired impact.

"I've said previously that I believe that it is in China's interest to allow its currency to move up, largely because its procedures that it uses to support its currency requires that their central bank accumulate very large quantities of U.S. Treasury securities," he said.

"Unless they sterilize that very substantial inflow, they create significant distortions in their financial system, and ultimately it could be very serious for the Chinese economy. They know that, and they have said that they intend to adjust their currency. The issue that seems to be on the table is when and that -- what is the nature of the changes."

The adjustment of the exchange rate is only slight, but China's central bank, the People's Bank of China, seemed to indicate that the adjustment is only the first step in a gradual move toward a looser exchange-rate regime.

"For the present stage," the bank said in a statement, the yuan will be allowed to move 0.3 percent up or down in value against the dollar, while the value of other currencies will also be allowed to move up and down within a range announced by the bank.

"The People's Bank of China will adjust the band of the exchange rate when appropriate, based on the maturation of the market and economic and financial circumstances," the statement read.

But it also stressed that the bank will focus on ensuring the "basic stability" of China's exchange rate and "protecting the stability of the macro-economy and financial markets."

Economists said China's initial revaluation will have little impact on world trade and America's growing trade deficit with China.

"At 2 percent vs. the greenback, this yuan revaluation is unlikely to affect the U.S. trade deficit with China or

any of China's trade flows or economic conditions at all," Carl B. Weinberg, chief economist of High Frequency Economics, wrote in a note to clients Thursday. "Local energy and commodity prices will come down a pinch, but the variations will be small. This is a nice token move, but it is no economic knockout."

U.S. Business and Industry Council president Kevin Kearns said, "The Chinese government figures it can placate its critics by budging the currency just a hair, but again this insignificant step is of no help to American's domestic manufacturers."

CHINA'S CURRENCY MOVE

• BEIJING'S ANNOUNCEMENT

China will stop pegging its currency, the yuan, to the dollar, succumbing to pressure from the U.S. and other trading partners. Instead, it will peg it to a basket of as-of-yet unnamed currencies.

• HOW IT WORKS

At the end of each day, China will announce an official price for the yuan which will be set as the midpoint for a 0.3 percent band in which the yuan will be allowed to trade the following day.

• SOUTH FLORIDA REACTION

George Feldenkreis, chairman and chief executive of Perry Ellis International, a Miami apparel maker that has most of its apparel stitched in Asia or Central America: "It's a step in the right direction. It shows at least that they are listening to the world, not only to the United States."

But Feldenkreis also said it would not affect his company, which instead faces 10 percent safeguard duties, a special import duty imposed when a flood of imports threaten to overwhelm a domestic industry. This has been the case of Chinese apparel imports.

He called the move political: "This is going to be a quid pro quo, for the Chinese government to say, 'We did what you wanted, now take off the safeguards.' "

Feldenkreis added that the move will be good for the world economy because the undervalued Chinese currency has been distorting trade patterns, making manufacturing exports from many countries uncompetitive. The only danger is that a strong revaluation will make Chinese goods more expensive and would have the perverse affect of increasing the U.S. trade deficit with China, which is already growing rapidly.

Keith Koenig, City Furniture president: "Any unfavorable exchange rate change in the Chinese currency will cause retail prices of imported furniture from China to go up and that will be unfavorable to the American consumer. It might help improve domestic production although that is to be determined."

Koenig, whose company is based in Tamarac, said that a higher exchange rate will raise prices for imports in this country and said that the Chinese furniture makers his company deals with might have a problem absorbing the higher prices, but that the change might offer a hand to other countries which were uncompetitive with Chinese prices.

-- JANE BUSSEY