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Public Announcement of the People's Bank of China on Reforming the RMB Exchange Rate Regime

July 21, 2005

With a view to establish and improve the socialist market economic system in China, enable the market to fully play its role in resource allocation as well as to put in place and further strengthen the managed floating exchange rate regime based on market supply and demand, the People's Bank of China, with authorization of the State Council, is hereby making the following announcements regarding reforming the RMB exchange rate regime:

1. Starting from July 21, 2005, China will reform the exchange rate regime by moving into a managed floating exchange rate regime based on market supply and demand with reference to a basket of currencies. RMB will no longer be pegged to the US dollar and the RMB exchange rate regime will be improved with greater flexibility.

2. The People's Bank of China will announce the closing price of a foreign currency such as the US dollar traded against the RMB in the inter-bank foreign exchange market after the closing of the market on each working day, and will make it the central parity for the trading against the RMB on the following working day.

3. The exchange rate of the US dollar against the RMB will be adjusted to 8.11 yuan per US dollar at the time of 19:00 hours of July 21, 2005. The foreign

exchange designated banks may since adjust quotations of foreign currencies to their customers.

4. The daily trading price of the US dollar against the RMB in the inter-bank foreign exchange market will continue to be allowed to float within a band of ± 0.3 percent around the central parity published by the People's Bank of China, while the trading prices of the non-US dollar currencies against the RMB will be allowed to move within a certain band announced by the People's Bank of China.

The People's Bank of China will make adjustment of the RMB exchange rate band when necessary according to market development as well as the economic and financial situation. The RMB exchange rate will be more flexible based on market condition with reference to a basket of currencies. The People's Bank of China is responsible for maintaining the RMB exchange rate basically stable at an adaptive and equilibrium level, so as to promote the basic equilibrium of the balance of payments and safeguard macroeconomic and financial stability.

Objective of the Monetary Policy

The objective of the monetary policy is to maintain the stability of the value of the currency and thereby promote economic growth.

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中文版

Jun,13,2008

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Monetary Policy Instruments

The monetary policy instruments applied by the PBC include reserve requirement ratio, central bank base interest rate, rediscounting, central bank lending, open market operation and other policy instruments specified by the State Council.

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中国人民银行
THE PEOPLE'S BANK OF CHINA

中文版

Jun,13,2008

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Monetary Policy Committee

Article 12 of the Law of the People's Republic of China on the People's Bank of China provides " the People's Bank of China is to establish a monetary policy committee, whose responsibilities, composition and working procedures shall be prescribed by the State Council and shall be filed to the Standing Committee of the National People's Congress. The Monetary Policy Committee shall play an important role in macroeconomic management and in the making and adjustment of monetary policy."

Rules on Monetary Policy Committee of the People's Bank of China stipulates that the Monetary Policy Committee is a consultative body for the making of monetary policy by the PBC, whose responsibility is to advise on the formulation and adjustment of monetary policy and policy targets for a certain period, application of monetary policy instrument, major monetary policy measures and the coordination between monetary policy and other macroeconomic policies. The Committee plays its advisory role on the basis of comprehensive research on macroeconomic situations and the macro targets set by the government.

The Monetary Policy Committee is composed of the PBC's Governor and two Deputy Governors, a Deputy Secretary-General of the State Council, a Vice Minister of the State Development and Reform Commission, a Vice Finance Minister, the Administrator of the State Administration of Foreign Exchange, the Chairman of China Banking Regulatory Commission, the Chairman of China Securities Regulatory Commission, the Chairman of China Insurance Regulatory Commission, the Commissioner of National Bureau of Statistics, the President of the China Association of Banks and an expert from the academia.

The Monetary Policy Committee performs its functions through its regular quarterly meeting. An ad hoc meeting may be held if it is proposed by the Chairman or endorsed by more than one-third of the members of the Monetary Policy Committee.

The opinions expressed in the meeting of the Monetary Policy Committee will be recorded in the form of "meeting minutes". Such minutes or any resulted policy advice, if approved by more than two-thirds of the members of the Monetary Policy Committee, should be attached as an annex to the proposed decisions of the PBC on annual money supply, interest rates, exchange rates or other important monetary policy issues to be reported to the State Council for approval. In the case the PBC files its decisions on other monetary policy related issues with the State Council, it should enclose the meeting minutes or policy advice of the Monetary Policy Committee at the same time.

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FROM THE OFFICE OF PUBLIC AFFAIRS

September 3, 2003
JS-692

Press Roundtable Transcript with Treasury Secretary Snow in Beijing, China on September 3, 2003."

SNOW: Thank you very much Mr. Ambassador. Thank you very much for all your kindness and hospitality during our visit. The ambassador and I have been spending a great deal of time together, as we have called upon the economic and political leaders of your great country.

Let me say that we have had a series of very good meetings, very important meetings and, to me, very encouraging meetings. So, let me begin by thanking my hosts for inviting me to Beijing – me and my colleagues from the Treasury Department – to discuss issues of mutual interest to our two countries. I've been to China many times in the past in a private capacity, as a businessman. This is my first opportunity to be here in my new capacity as a representative of the United States government. I want to state how much I appreciate the hospitality and the warmth and the friendship that has been extended to us, to me and to the Treasury delegation, throughout the course of our discussions. I am honored this afternoon to have the opportunity to continue those discussions with the premier, with Premier Wen. In all of these discussions I have found the Chinese leaders open, frank and encouraging of the close ties and the close working relationship between our two countries.

Early last year when President Bush visited China and met with President Jiang Zemin, President Bush said, and I want to quote him here because I think his quote sets the foundation for this relationship. He said, "China and the United States, both with significant influence in the world, should step up dialogue and cooperation, properly handle their differences, and work together to move the constructive and cooperative relations between us further forward." Our talks this week are fully in keeping with the spirit of President Bush's comments.

One thing is clear and that is economic engagement and extending the engagement between the United States and China will promote prosperity in both of our countries and, in addition, for all of our trading partners. Our trade with you makes your economy stronger. Your trade with us makes our economy stronger. As our economies are stronger, benefits are extended to the rest of our trading partners. So just as China benefits from our market, U.S. businesses and consumers should benefit from China's growth. Clearly, investments and technology from the United States help to sustain high growth in China.

In recent years, China has made historic strides in reforming its economy and moving to a market-based system. We applaud that and urge continued progress.

It's been our view for some time that the best international economic system, the best for China, and the best for the United States, and the best for the whole trading world is one based on the principle of free trade, open markets, free capital flows, and market-based exchange rates, among the major economies. China is now clearly one of the major economies of the world. It's with these principles in mind, these ideas in mind, that I am here to discuss our economic relationship with the Chinese leaders and to encourage China to continue to take advantage of its strong growth to accelerate progress in all of these areas. The growth which China has enjoyed makes it easier to move further in the direction of open markets and floating exchange rates and free capital flows and to advance these ideas within the

economy of China for the benefit of the Chinese people.

It's important to recognize that the United States is committed to a growing, healthy and mutually beneficial trade relationship with China. In that regard, it's very important that China continue its efforts to fully implement the commitments it made to the World Trade Organization. Progress on market opening should be made for products such as soy beans, which is important to the United States, of course, but important to the citizens of China as well. We also encourage further relaxation of the ownership rules in the area of financial services.

Another area of concern for me is that U.S. companies continue to lose billions of dollars because of the piracy of intellectual property. Enforcement of the good intellectual property laws which China has put in place is essential to our continued economic relationship.

Another area that is important is the free flow of capital. The free flow of capital is a fundamental component of our global system of international trade and international finance. While I applaud and welcome the recent policy changes that allow for greater capital mobility, it's in China's interest to accelerate these efforts. For example, it would be beneficial to expand the qualified institutional investor programs, to increase both portfolio inflows and portfolio outflows. It would also be advantageous to liberalize the long-term debt transactions, and overall to create open capital markets. As we talked to the Chinese economic leaders we emphasized over and over the necessity to develop open capital markets. They really are the key to the success of a market-based economy.

Finally, let me turn to the subject of exchange rates, because the subject of exchange rates has also been much in discussion among us. The establishment of flexible exchange rates, of a flexible exchange rate regime, would benefit both our nations as well as our regional and global trading partners. Market-determined floating currencies are really the key to a well-functioning international financial system. For the world's major traders, only freely floating currencies bring the accuracy and the efficiency necessary for the proper pricing account settlement in capital flows. That's really our central point, that floating rates, market-based, flexible exchanges create the signals for a well-functioning flow of resources on a global basis. There's ultimately no substitute for that.

We've learned over the years that rigidities of all kinds, including rigidities in exchange rate mechanisms, tend to distort the proper functioning of markets. Open competitive markets with little or no interference are essential. They are really needed to insure that people and investment capital can seek out the best ideas and opportunities.

How do economies grow? How do they prosper? They grow and prosper by bringing people with ideas together with people with capital. Then, seeing those ideas flower in the marketplace, with new products and new services. That's the engine of growth, and it requires the availability of capital and it requires markets that make capital available to those entrepreneurs and businesses that generate the ideas and will employ people and bring people and capital together.

So progress on each of these issues, in our view, will yield long-term benefits for the peoples of China, the peoples of the United States and the peoples of the world. This is clearly a win-win situation for China and the United States; a win-win situation brought about by embracing these ideas of open markets, capital flows, floating exchange rates.

During my meetings this week I expressed these views with the Chinese economic leaders. On the need for currency flexibility, in particular, I was encouraged. I was encouraged to hear the reaffirmation of China's longstanding goal to move toward greater flexibility. In the course of those discussions I was repeatedly assured that interim steps are now being taken and progress in this area will continue.

In order to continue this dialogue, in order to further communications and understanding between our nations on this issue and other important economic, financial and trade issues, I yesterday extended an open invitation to host the Vice-Premier, Huang Ju, and other officials to come to Washington to continue the work on these important matters.

We also intend to appoint a Treasury Attaché at the U.S. Embassy in Beijing where the Ambassador tells me that that Treasury person will be well cared for, and looked after, and will an important part of the Ambassador's team. Let me conclude by saying that I look forward to our continued discussions as we cooperate to enhance our economic relationship.

So I thank you very much and now look forward to your questions:

QUESTION: When you talk about these interim measures on the currency, what measures specifically are you talking about, and what concretely do you expect to leave here with?

SNOW: Well, we have in mind things like expanding the opportunities for capital flows, expanding the opportunities for ownership of financial assets. We have in mind things that are underway already, being expanded and accelerated, removing some of the burdensome capital requirements in the banking system, capital asset ratio requirements; and ownership rules, relaxation of ownership rules; a variety of things in this area.

QUESTION: On currency though, specifically? Interim measures?

SNOW: Right, well these are interim measures that prepare the economy for a floating exchange rate system, that get it ready for a floating-exchange system. That was the nature of a lot of our dialogue, the interim steps, putting in place the interim steps that prepare the way for an effective floating regime.

QUESTION: Do you have a timetable for these interim measures?

SNOW: Well they're underway right now, and we're pleased to see them underway. We want to see them accelerate. Our conversation yesterday with the economic leaders indicated that more is coming, and we urged that on, we urged them on with doing more.

QUESTION: And could you tell us were the Chinese receptive to your ideas, I mean the incentives for them to adopt these moves?

SNOW: The incentives are their own advantage. It's in China's advantage to open its system up. It's in China's advantage to encourage greater flows both in and out. It's in China's interest to secure a more market-based set of financial institutions. And, as China moves down this path, it prepares the way to move to floating rates. That was the essence; that was an important part of our discussion yesterday.

QUESTION: Could I ask you to be a little specific about this? Was it in essence these interim measures attempted to rebalance the demand between the renminbi and the dollar? Specifically was it to allow more Chinese companies to invest in U.S. Treasuries, and do they also mention allowing domestic Chinese companies or funds to invest in stock markets abroad?

SNOW: Yes. It's not. No further actions need to be taken to allow foreign investment in the United States bond market. It's an open market, so any restrictions would be local restrictions not U.S. restrictions of course. But we had that discussion of opening up opportunities for investments going both ways, in both the financial arena and in the non-financial arena.

QUESTION: I'd like to ask a question about the trade relations between the two sides. The American trade deficit with China has attracted much attention from your side for a long time. As we know, with the development of trade liberalization and economic globalization, I think that it's not so important to just talk about bilateral trade surplus or deficit. For example, China has several thousand billion dollar U.S. trade surplus with the United States, but she also has an approximately forty billion U.S. dollar trade deficit with the other Asian countries like Japan and Malaysia and the Republic of Korea. And this offsets the surplus with the U.S. At the same time, China has a trade surplus with the United States. She also purchases a large amount of American debt, which offer a great support to the American economy. So can we say that the trade relations between the U.S. and China are not only just bilateral trade relations, but are also multiparty and mutually beneficial relations on

the global trading system? What we should do is to develop this win-win or multi-win trade relations. Do you agree with that?

SNOW: I'm not sure I fully understand the question, but let me try and respond as best I do understand it. The United States and China have a good trade relationship. We benefit from the opportunity to have low-cost goods from China in the United States and you benefit from the opportunity to take advantage of U.S. exports. We'd like to see that trade deficit narrowed though. I think it's unsustainably large at current levels. One way for it to narrow is for the domestic economy of China to strengthen. Because as it strengthens, then with more disposable income in China, there will be an increase in the propensity to buy U.S. goods, and that would be healthy. So we are urging the Chinese officials to continue with their reform strategies, because those reform strategies, if persisted in, if continued, will clearly create a stronger domestic economy. That's in China's interest and it's very much in the U.S. interest as well. We're interested in selling more products and services in China. China will benefit from that, just as you benefit from access to our markets.

QUESTION: I take it from your choice of language that you would say that China is not at this moment ready for a free floating currency. Am I correct in that assumption, and if they're not ready now, what specifically do they have to do? How long will it take?

SNOW: Well, the objective here is to get a commitment to move to a free-floating currency. That's what we want. We'd like to see China operating in a regime of market-based, floating, flexible exchange rates. And as I said in my comments, I was encouraged to see the Chinese officials reaffirm that objective, that policy goal. I was also pleased to see them making strides on the interim steps that have to be put in place. I don't think it's helpful for us to try to talk about a timetable. I do think it's helpful though to see that reaffirmation of the policy direction, and to see the progress that's being made in the commitment to further progress on these interim steps.

QUESTION: Mr. Secretary could you tell us if you discussed at all any specific sectors of trade, U.S. sectors of trade, textiles, furniture, or shoes or any of the other sectors where there's been some political pressure in the Unites States to do something about China trade? Did any of your Chinese hosts discuss any specific measures that they might take to address any concerns in those specific sectors?

SNOW: Well our discussions were more general I would say than sector-specific, although the financial sector did receive a good deal of specific attention, because a focal point of our conversations was moving towards flexibility in exchange rates. It's the freeing up and opening up of the financial sector which is part and parcel of moving to fluctuating rates. But we did talk generally about opening up markets in other areas, about the intellectual property rights and better enforcement there; about making the market more open for soybeans; and, as I say, financial services; and agriculture in general. So there was a general discussion of other areas and a more specific discussion of financial services.

QUESTION: The National Association of Manufacturers says that China maintains an artificially low exchange rate that is the single biggest factor in manufacturing job loss in the U.S. and I'm wondering if you consider the Yuan undervalued. If so by how much? And what relationship does that have to the loss of jobs in the U.S.?

SNOW: What we're seeking is broad movement to flexibility so that markets can be allowed to set values. We're placing our confidence in markets. The only way ultimately to know the answer is to place your confidence in markets. Therefore I'm encouraged by what I heard. We want to make sure that you use markets so that there isn't any artificial propping up of one sector or another, so the U.S. manufacturers will have a fair opportunity to compete on a level playing field.

QUESTION: I would like to ask: you are going to have a meeting with Premier Wen Jiabao this afternoon. What are the topics that you are especially interested in during your meeting with the Premier?

SNOW: It'll be a continuation of the subjects we've reviewed here. I will commend the Premier on the enormous progress that 's being made in this economy. I will

commend him on the reforms that are underway. I will reaffirm the importance of this relationship. I will let him know that we want to see a win-win relationship between China and the United States. I will tell him that we have an enormous amount to gain together, working together. I will urge him on with the reforms and indicate specifically our interest in seeing a movement to more open capital flows; applauding China's WTO commitment, open banking and insurance markets, to foreign services; indicate that some problems remain. We'd like to see continuing progress in this area. I'll suggest to him that it's in China's interest to adopt flexible, risk-based capital requirements for the banking sector. I will indicate our interest in seeing China move forward and honor the commitments it's made to allowing branching by non-life insurance companies, financial services companies. I will urge, as well, continued progress on securities and asset-management, including importantly allowing a majority ownership by foreign firms.

We see more robust capital markets, more market-based capital markets as an essential component of the China of the future. In saying that, our position is it's in China's interest to move in that direction. I will suggest to him our interest in seeing China move towards a floating rate, a flexible regime of international currencies.

In addition, at some point our conversation will turn to terrorist finance, and I will commend the Premier for China's cooperation in dealing with the threat of terrorist finance. The United States, with China and other nations of the civilized world, are committed to dealing with the terrorist threat. An important component of dealing with terrorism is dealing with terrorist finance. I want to reaffirm our mutual commitments to do that. And of course I will thank the Premier on behalf of the President for the leadership China is showing in dealing with the threat of nuclear arms on the Korean Peninsula.

QUESTION: I have two questions. One is: many analysts blame this round of the Japanese economic recession on the Plaza Accord 1985. I want to know: do you agree with that? Meanwhile I would like to know your opinion on how the foreign exchange rate influence could be used to resolve the trade deficit.

SNOW: Fluctuating exchange rates, if they're really used, provide a mechanism for the adjustments that need to be made so that imbalances aren't sustained in the world economy. That's really why we want to use flexible exchange rates. If a country has a surplus, and it goes on for quite a while, the fluctuating exchange rate mechanism will provide for an adjustment process as currencies change values. If a country is in long-term deficit, the exchange rate mechanism will provide for an adjustment of currencies which will correct it. The virtue of fluctuating rates is that the price signals are working to create a healthy and efficient, continuous adjustment process. Where fluctuating rates, market-based rates, are impeded, imbalances develop in individual economies and they develop in the world trading system. So the world trading system is more efficient. It works better. It works better under a regime of fluctuating exchange rates. So that's why we will be urging the authorities to move in that direction, and to take the steps that prepare the way for the implementation of a fluctuating, market-based regime of currencies.

I thank you very much for this opportunity to be with you and respond to your questions.

FROM THE OFFICE OF PUBLIC AFFAIRS

September 21, 2003
JS-755

United States Treasury Secretary John W. Snow
Statement to the International Monetary and Financial Committee (IMFC)
Dubai, UAER
September 21, 2003

The balance of risks to the global economy has improved since we met in Washington this spring. While uncertainties have eased and recovery is strengthening in some regions, we cannot relax. We must continue to strive for higher economic growth.

This is the message I delivered to my colleagues in Japan earlier this month, and in Europe over the summer. We must all work together to ensure a strong, broad-based, and sustained upturn in the global economy.

On the demand side, appropriate monetary and fiscal policies are already in place in many of the key economies. But the success of the agenda for growth will depend on improving economic structures that raise productivity and provide a lasting basis for a durable recovery in private sector activity. Important steps have been taken – for instance to reduce marginal tax rates, reform labor markets, strengthen financial systems and stimulate investment. We now need to build on this progress. The rewards of taking decisive action now will be sizable in the long run.

The U.S. recovery is gaining momentum, and I expect growth to accelerate in the latter half of this year. In fact, a recent Wall Street Journal survey of economists predicts growth of 4.7% in the second half of this year.

Yet the global economy cannot continue to rely on the United States alone to power the global growth engine. Industrial countries must take additional action to address remaining structural impediments to long-term growth. Emerging markets, which are benefiting from benign external financing conditions, should seize the opportunity to consolidate reform. Finally, we all need to act to avail ourselves of the benefits of open trade – with the international financial institutions helping as needed to build trade capacity and facilitate adjustment.

A Global Growth Agenda

Through sound advice and strong support for reforms, the IMF can help foster financial stability and promote economic growth. The IMF needs to focus on its core strengths, coordinating with the World Bank, other international institutions, and bilateral donors in order to achieve results.

Promoting Crisis Prevention and Resolution

The number and severity of crises in recent years has diminished, and flows into emerging markets' debt have risen. Yet foreign direct investment is likely to fall to a seven-year low this year. Neither we, nor the IMF, can afford to be complacent. The IMF has taken some key steps in the last year, but more needs to be done.

The IMF must do a better job of analyzing vulnerabilities and predicting crises. Good work has been done to improve analysis of debt sustainability. Now the IMF should follow up on currency mismatches and balance sheet impacts. And the Fund needs to focus on providing a candid and fresh approach in all its surveillance

activities.

Wider dissemination of IMF analysis is essential to achieving the goals of stability and growth. It will be critical that members and IMF management work together to strengthen IMF transparency, especially the publication of all exceptional access documentation and a separate justification of occasions of exceptional access. More information will help the market and public at large understand and respond to reforms, and greater transparency will make the IMF itself more accountable, and over time further enhance the quality of the analysis. I urge all countries to publish their surveillance documents.

Official resources are limited, and there will not be a quota increase in the foreseeable future. Neither large scale nor repeated access to IMF lending will itself solve any country's economic challenges. The IMF made an important decision earlier this year by developing procedures to govern exceptional access to Fund resources. These rules make the role of the official sector in crisis resolution more predictable. We should now seek to raise the bar for lending standards, with the goal of reducing the number of IMF programs.

I want to reflect briefly on a key development this year that has made the debt restructuring process more orderly and predictable. Collective action clauses are now standard in internationally-issued sovereign debt. We commend the countries that have issued external bonds with these clauses. We hope that future issuers will follow this important trend in strengthening market practices.

Promoting Growth in Low Income Countries

The IMF's principal role in low income countries should be macroeconomic surveillance, monitoring and technical assistance. Many low income countries have attained macroeconomic stability.

The IMF will be considering its role in low income countries over the next few months. It is important for the Fund to support countries that have good policies in place. I want to challenge the IMF to more clearly define the scope and terms for its support to low income countries and to consider transforming PRGFs from loans to grants.

Finally, I want to underscore that the United States supports a strong role for developing countries and emerging market countries in the international financial system.

We also believe, however, that quotas should reflect economic weight and the ability to contribute to the financing of the IMF. As the world has changed, some countries are now under-represented, and some carry too much weight. There is merit in discussing potential changes, but we recognize that quota redistribution is only likely in the context of a general quota increase, and the Fund's current ample liquidity does not require such an increase. To help developing countries enhance their participation in decision making, we have strongly supported measures to improve the capacity and influence of governments and their Executive Board representatives.

Assisting Iraq

The IMF must play an integral role in facilitating the reconstruction and recovery of Iraq. I look forward to next month's meeting in Madrid as an opportunity for the international community to demonstrate its sustained commitment. The IMF should be prepared, expeditiously, to provide its expertise and financial support.

Combating Terrorist Finance and Money Laundering

Protecting the world's financial systems from abuse by terrorists and money launderers protects our citizens. We have made good progress over the past 24 months, and this reflects to a significant degree the hard work of many of those attending this session. I especially want to commend the IMF, along with the World Bank and FATF, for their important and ongoing contributions in the fight against

terrorist financing and money laundering, and I look forward to the AML/CFT assessments becoming a permanent part of the IFI's oversight and surveillance of financing systems.

Our successes, however, cannot blind us to the long road that remains ahead. We cannot yet say that we are fully denying terrorists access to the formal networks of international finance (or capital flows) – and we cannot be satisfied even when we do. Remittances are an important source of income for many poor people. However, at times, the channels through which remittances flow lack the transparency of the traditional financial sector, rendering those channels vulnerable to abuse by terrorists and money launderers. We must work to reduce the risk of abuse of informal remittance channels by encouraging a further deepening of the formal financial system – a win/win measure that will benefit developing countries and emerging markets. Above all, we must cut off terrorist financing at its source. Our next steps should include making national asset freezing regimes more effective, extending safeguards to informal financial sectors, addressing the inadequacies in our formal sectors that drive legitimate customers elsewhere, and ensuring that charitable donations go for worthy causes, not to support terror.

Penolakan China..., Eflina Pehulita Sinulingga, FISIP UI, 2008

FROM THE OFFICE OF PUBLIC AFFAIRS

October 1, 2003
JS-774

"China's Exchange Rate Regime and its Effects on the U.S. Economy"
John B. Taylor Under Secretary of Treasury for International Affairs
Testimony
before the Subcommittee on Domestic and International Monetary Policy, Trade, and Technology House Committee on Financial Services
October 1, 2003

Chairman King, Ranking Member Maloney, Members of the Subcommittee, thank you for giving me the opportunity to testify on China's exchange rate regime and its effects on the U.S. economy.

This is the fifth time that I have appeared before this Subcommittee as an Administration witness. Each time I have been asked to focus on an important facet of our international economic policy. I have testified on our policy toward emerging markets, on our policy for developing countries-including reforms at the Multilateral Development Banks and the new Millennium Challenge Account, and on our policy to remove barriers to the free flow of capital in our trade agreements-including those with Singapore and Chile. In each of these cases, an underlying goal of our policy has been to raise economic growth and increase economic stability around the world, and in doing so benefit the American people with more jobs, more security, and a better life. My testimony today on China's exchange rate regime will be no different in this respect.

The Overall International Economic Strategy for Growth and Stability

The Administration's major economic endeavor now is to strengthen the economic recovery in the United States. The President's Jobs and Growth package, enacted into law this summer, was essential, as are his proposals for tort reform, regulatory reform, and health care reform. But there are barriers to economic growth and stability in other countries- in Europe, in Asia, in Latin America, in Africa-as well as in the international trade and financial systems that have important implications for growth in the United States.

This is where our overall international economic strategy fits in. Our policy toward China-and China's exchange rate regime in particular-is part of that overall strategy. The strategy has been to urge the removal of rigidities and barriers wherever they exist, and to encourage pro-growth, pro-stability policies that benefit the U.S. and the whole world. It is a two-track approach-domestic and international. The international component is applied bilaterally and multilaterally.

Progress on Growth and Stability

I am pleased to report that this endeavor is working. Thanks to the fiscal and monetary policy responses, economic growth in the United States is picking up significantly now after the severe shocks of the terrorist attacks, the corporate accounting scandals, and the stock market drop of 2000. Global growth is also improving. There is more evidence of stronger economic growth in the world's second largest economy, Japan, and in Canada and the United Kingdom, as well as several emerging market countries.

There is also a notable improvement in economic stability around the world, despite the uncertainties about terrorist attacks and the ongoing war against terror. The number and severity of financial market crises are down, capital flows are up, and interest rate spreads are down compared with the late 1990s. This improvement in global economic stability is important for the United States. Greater economic stability is essential to creating a long lasting recovery, which is needed for sustainable job creation.

Agenda for Growth

Despite this progress on the growth and stability front, we need to do more. During the summer months, Secretary Snow embarked on an international pro-growth tour starting in Europe, continuing on to Asia (including China as I will shortly discuss in more detail), and culminating in the annual meetings of the World Bank and the IMF in the Middle East where he forged an agreement on a new "G7 Agenda for Growth." This milestone agreement creates for the first time supply side surveillance - a process of benchmarking and reporting in which each G7 country takes actions to spur growth and create jobs. It focuses on supply-side policies that increase flexibility and remove structural barriers to growth, because such policies are most needed to raise growth among our G7 partners, especially those in the European Monetary Union. For its part the United States will work to lower health care costs, reduce frivolous lawsuits, and streamline regulations and needless paperwork. The other G7 countries are endeavoring to implement other supply side policies. For example, Germany is focusing on labor, health, and pension reforms.

Our engagement to foster pro-growth, pro-stability policies extends to the emerging markets and developing countries. For example, we recently created a new United States-Brazil "Group for Growth" through which the two countries will work together to identify pro-growth strategies at the micro as well as macro levels. And the Millennium Challenge Account is aimed at encouraging pro-growth policies in the developing countries. Our reforms also call on the World Bank to encourage economic growth by using IDA funds for the private sector as, for example, in the new IDA/IFC small business loan program for Africa. And we will continue to promote trade through the bilateral, regional, and global trade agreements. While the outcome at Cancun was a missed opportunity for global trade liberalization, our free trade initiatives, including the U.S. proposal to cut tariffs to zero in manufacturers will continue.

Policy Principles Regarding Alternative Exchange Rate Regimes

Exchange rate policy also has bearing on growth and stability. The move by several large emerging market countries-such as Brazil, Korea, and Mexico-to flexible exchange rates combined with clear price stability goals and a system for adjusting the policy instruments is one of the reasons we are seeing fewer crises and greater stability.

We emphasize that the choice of an exchange rate regime is one where country ownership is particularly important. We also recognize that, especially in the case of small open economies, there are benefits from a "hard" exchange rate peg, whether dollarizing, as with El Salvador, joining a currency union, as with Greece, or using a credible currency board, as in Bulgaria or Hong Kong.

The Economy of China

With this context, let me now address China's economy and its exchange rate regime. Economic reforms in China have increased economic growth and have made China one of the largest economies in the world. China is now a major economy, and it is still growing rapidly. It is already an engine of global growth. With per capita income of only about $1,000 per year and with financial, legal and

regulatory systems in need of reform, China still faces challenges in its effort to catch up with developed economies.

China's Exchange Rate Regime

For nearly ten years now, the Chinese have maintained a fixed exchange rate for their currency, the yuan, relative to the dollar. The rate has been pegged at about 8.28 yuan/dollar for the entire period. Thus, as the dollar has appreciated or depreciated in value relative to other currencies, such as the Euro, the yuan has appreciated or depreciated by the same amount relative to these other countries.

To maintain this fixed exchange rate, the central bank of China has had to intervene in the foreign exchange market. It sells yuan in exchange for dollar denominated assets when the demand for the yuan increases and it buys yuan with dollar denominated assets when the demand for the yuan decreases. Recently the central bank has intervened very heavily in the markets to prevent the yuan from appreciating. Since the end of 2001, dollar buying has been so great that the foreign reserves held by the Chinese government have risen by $153 billion to over $360 billion.

This accumulation of foreign exchange reserves would tend to expand China's money supply, although in recent months the Chinese central bank has moved to reign in monetary expansion. Among other measures to sterilize reserve accumulation, the central bank has - for the first time - begun issuing central bank paper to restrict growth of the monetary base. Nevertheless, the broader money supply continues to grow very rapidly: M2 climbed 22 percent over the 12 months ending in August 2003.

It is also important to recognize that China still has significant capital controls. China's capital controls allow for more inflows than outflows, thus bolstering foreign exchange reserves. China is gradually loosening some controls (on securities rather than debt), and outflows are likely to grow as new channels develop for Chinese to seek diversification and better returns than those offered by low domestic interest rates. Indeed, there is already significant leakage of capital. A relaxation of controls on outflows would reduce upward pressure on the yuan.

Impact on the United States

U.S. imports from China are equal to about 1 percent of U.S. GDP, or 11 percent of total U.S. imports. Although this share may seem small, China's imports to the U.S. have been increasing rather rapidly, between 20 and 25 percent in recent years and months. In general, these imports result from China using low-skilled labor to assemble and process imported parts and materials originating in other countries-mostly from other Asian countries that have traditionally exported directly to the U.S. Consequently, the share of U.S. imports from these other countries has declined just as China's share has increased. Asia's share of U.S. imports has declined slightly. Much of the increase in U.S. imports from China has come at the expense of imports that once came directly from other Asian countries.

At the same time, growth of U.S. merchandise exports to China has been accelerating recently and grew 22 percent in the first 7 months of this year. Growth has been especially rapid in recent years for U.S. exports to China of transportation equipment (including aircraft engines), machinery, steel-making materials, chemicals, and semiconductors.

China has a large trade surplus with the United States. However, because China has a large deficit with the rest of the world, it does not have a large overall current account surplus. China's bilateral trade surplus was $103 billion in 2002 with the U.S. while China's deficit with the rest of the world was about $73 billion. Thus, China's current account surplus was under 3 percent of GDP in 2002 and likely to

decline to less than 2 percent in 2003. Many imports from China are goods from other Asian economies that are processed or finished off in China before shipping to the United States. Other East Asian economies increasingly send goods to China for final processing before they are shipped to the United States. China accounted for 11 percent of U.S. imports in 2002, up from 3 percent in 1990. Meanwhile, the combined share of Japan, Korea and Taiwan declined to 17 percent from 27 percent over the same period.

The overall trade deficit of the United States is spread across many countries of the world in addition to China. For instance, the overall trade deficit reached $468 billion last year with 1) the Americas accounting for $105 billion, 2) Western Europe $89 billion, 3) Japan $70 billion, and 4) China $103 billion. The U.S. overall trade and current account deficit is due to the excess of investment over saving in the United States. If this gap were reduced through an increment in savings, the overall deficit could shrink as would the size of the bilateral deficits.

What impact would a change in the value of the yuan relative to the dollar have on the United States economy? An appreciation would make U.S. exports to China less expensive and it would make U.S. imports from China more expensive. The price of Chinese goods in the United States would not change by as much as the change in the exchange rate, because only a portion of most exports from China are produced in China, and because the retail price in the United States includes marketing, transport, and other logistical costs. And with a higher yuan, substitutes for Chinese products would likely come from countries other than China.

The United States Policy Position

With its rapid growth and substantial foreign exchange reserves, China is now in a position to show leadership on the important global issue of exchange rate flexibility. China represents one of the largest economies in the world, and a flexible exchange rate regime would be a good policy for China. It would allow China to open the nation to capital flows and reduce macroeconomic imbalances.

We have also been urging the Chinese to build on their strong record of economic reform by moving forward in two other areas: reductions in barriers to trade and capital flows. In the area of trade, it is important for China to fully implement, and even surpass, the commitments it made to the World Trade Organization. Tariffs on manufactured goods are scheduled to come down from an average of about 17 percent to an average of about 9 percent. This will still be well above the average of the United States and other large economies, which stand at about 4 percent. It is important that China continue to reduce its tariff barriers. It should also open its markets to agricultural products such as soybeans, as well as effectively enforcing intellectual property laws.

China's restrictions on capital flows are one of the major rigidities interfering with market forces. The authorities understand this and are beginning to reduce barriers to capital flows and develop more open and sophisticated capital markets. In fact, China has taken a number of steps in this area recently, including developing measures that will allow for some cross-border portfolio investment. At the same time, the Chinese authorities are working to strengthen the banking system and liberalize capital flows in order to prepare for a more flexible exchange rate.

Secretary Snow encouraged each of these steps in his trip to Beijing last month. He met Premier Wen, Vice Premier Huang, Central Bank Governor Zhou and Finance Minister Jin. In all his meetings discussions were detailed and candid. He also stated publicly, "the establishment of flexible exchange rates, of a flexible exchange rate regime, would benefit both our nations as well as our regional and global trading partners." The Chinese reported that they intend to move to a market-based flexible exchange rate as they open the capital account.

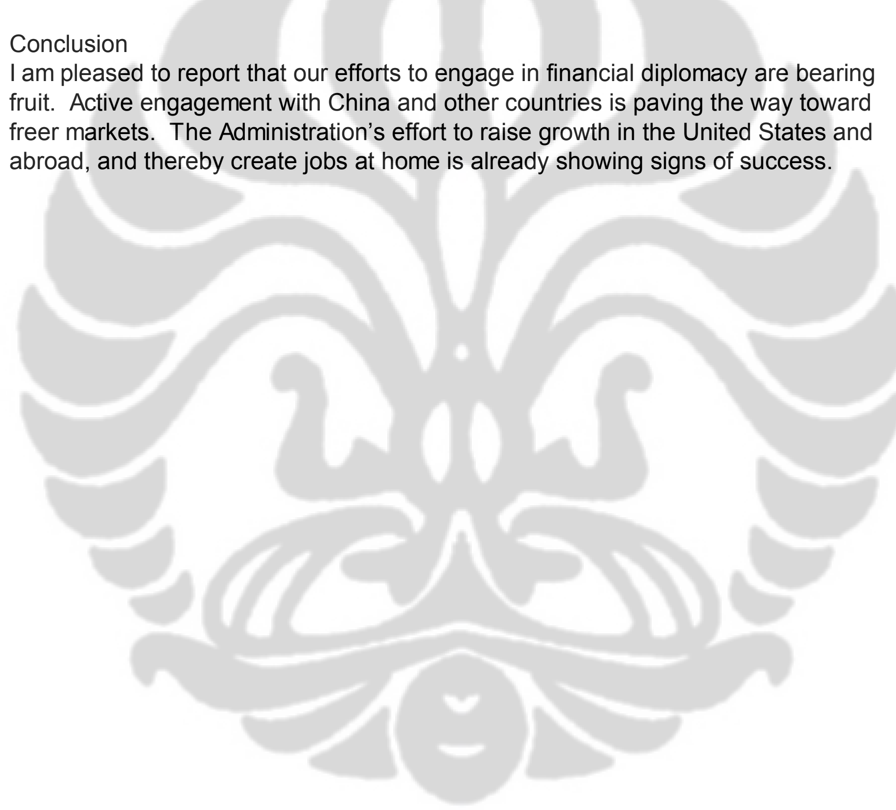
Secretary Snow's visit to Beijing was associated with announcements by China's central bank, including liberalized regulations for foreign firms managing their foreign exchange and significantly liberalized provisions to allow Chinese travelers to take foreign currency out of the country and to do so more frequently. We will continue to urge the Chinese to make rapid progress in these areas.

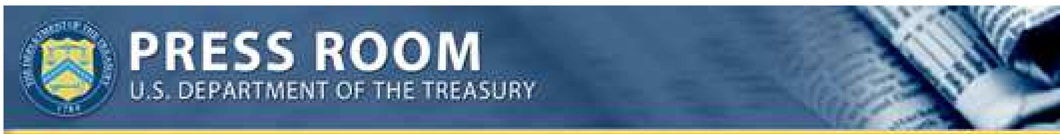
We are working on a possible technical cooperation agreement in the financial area. We intend to continue the high level conversations on this subject begun by Secretary Snow.

In addition, following Secretary Snow's visit, the Chinese and the G7 agreed to engage in talks about economic issues. This represents another example of how China, the U.S. and other affected parties can come together to work on an issue of vital interest to them all. The first meeting between senior officials from the G-7 and China's finance ministry and central bank took place last week in Dubai, where the Chinese economy, the G7 economies, and other economic issues, were discussed. Further meetings will be scheduled on a regular basis with China, the United States and the other G7 countries. After the Dubai meeting, China's central bank representative said that China is moving as fast as it can in its reform.

Conclusion

I am pleased to report that our efforts to engage in financial diplomacy are bearing fruit. Active engagement with China and other countries is paving the way toward freer markets. The Administration's effort to raise growth in the United States and abroad, and thereby create jobs at home is already showing signs of success.





FROM THE OFFICE OF PUBLIC AFFAIRS

October 30, 2003
JS-953

Testimony of Treasury Secretary John Snow
Before the Senate Committee on Banking, Housing and Urban Affairs

Chairman Shelby, Ranking Member Sarbanes, members of the Banking Committee, thank you for the opportunity to appear before you this morning to discuss Treasury's Report on International Economic and Exchange Rate Policies as well as related economic issues. The Report reviews developments in the United States and examines exchange rate policies in major countries across five regions – the Americas, Europe and Eurasia, Africa, the Middle East and South Asia, and East Asia. The Report documents the wide variety of exchange rate policies that are used around the world. A notable trend has been the move by many countries to adopt flexible exchange rates.

The Report concludes that no major trading partners of the United States meet the technical requirements set forth in the Omnibus Trade and Competitiveness Act of 1988. But let me be clear, the Bush Administration believes that the international trading system works best with free trade, the free flow of capital and with market-based exchange rates. An efficient system of trade and finance, with fair and enforced rules, is essential for the United States and all nations to maximize the benefits of trade and generate the highest levels of economic growth.

The Report finds that a number of countries continue to use pegged exchange rates and/or intervene in the foreign exchange market. It should be noted that a currency peg or intervention does not in and of itself satisfy the statutory test. Treasury has consulted with the IMF management and staff as required by the statute, and they concur with the findings of the Report.

The Bush Administration is aggressively encouraging our major trading partners to adopt policies that promote flexible market-based exchange rates combined with a clear price stability goal and a transparent system for adjusting the policy instruments. In my testimony today, I would like to discuss this work with you and the progress we are achieving.

Policies to Raise Economic Growth in the United States and the World

The Administration's international economic strategy aims for higher economic growth throughout the world. A stronger world economy is vital to sustaining U.S. economic growth and job creation. This is a reality of our increasingly interdependent world.

At the core of this strategy are the good economic policies we are implementing in the United States. But also at the core is our diplomatic work to encourage pro-growth and pro-stability policies in other countries. Good economic policies in other countries benefit the United States and the whole world. It is widely recognized throughout the world that free markets and market-determined prices are best able to allocate scarce resources to their most productive use. This is as true for domestic markets as it is for international markets. We strongly believe that the goals of raising growth and increasing stability can best be accomplished in an international financial system that relies on the principles of free trade, free capital flows, and market-based exchange rates among the major economies.

Free trade, in particular, improves the standard of living across countries. Thus, the Administration will continue to promote free trade through bilateral, regional, and

global trade agreements. In this respect, the outcome at Cancun was a missed opportunity. The United States stands ready to work with others who seek liberalization. Our free trade initiatives, including the U.S. proposal to cut tariffs to zero for manufactures, will continue.

Implementing this broad international strategy is an ambitious endeavor, but it is an agenda that the Bush Administration is determined to pursue. Convincing others to contribute to further improvement in global growth prospects is a top priority for the President. In furtherance of this agenda I traveled to Europe, China and Japan this summer to deliver this very message. Growth was also the key focus of my discussions with Asian financial leaders in Thailand. Change has already begun among several major economies. For example, Germany is pursuing critical labor market, tax and pension reforms under its Agenda 2010, and France is also moving forward through its Agenda 2006.

With President Bush's leadership, the Administration has made reform and economic growth a priority goal throughout the world. In addition to my own travel, Commerce Secretary Don Evans, United States Trade Representative Robert Zoellick and other senior Administration officials all continue to press nations to put in place pro-growth policies that will result in higher rates of productivity and growth both here and abroad

The Administration has urged Japan to implement comprehensive reforms to bring about lasting recovery. These reforms involve ending deflation, strengthening the banking system, and undertaking structural reforms that promote flexibility. Indeed, the Bank of Japan has aggressively increased the money supply to counter deflation, and the Koizumi government has made important headway on improving the health of the banking system.

Treasury is actively engaged with the Japanese on monetary, fiscal and exchange rate policies both bilaterally and through meetings of the G7 finance ministers and central bank governors.

At the recent G-7 meeting in Dubai, we made progress, gaining agreement on a new "G-7 Agenda for Growth." Under this milestone agreement, G-7 countries have committed to concrete structural reform actions to increase productivity, spur growth, and create jobs. And for the first time they have agreed to a process for benchmarking and reporting on their performance.

Each country will identify its own policy plan under the Agenda. For example, the United States will work to lower health care costs, reduce frivolous lawsuits and streamline regulations and needless paperwork through the President's Six Point Plan to promote economic growth. Other G-7 countries will implement policies appropriate to their situations. Countries in the European Union will be looking at further ways to revitalize investment and create jobs. Japan has reiterated its commitment to reform.

The Agenda for Growth must be about action and results, not just plans and platitudes. When we met in Dubai, my G-7 colleagues agreed to be ambitious in embarking on reforms and pursuing growth. In coming months, we will be working to evaluate proposals and assess the results of our efforts. As the United States assumes chairmanship of the G-7 in 2004 that focus will be maintained.The Administration is also engaging in other initiatives, both bilateral and multilateral, to advance growth and stability in emerging markets and developing countries. For example, Treasury is working with Brazil through a new "Group for Growth" to identify steps to expand economic potential; the Millennium Challenge Account targets assistance to countries that perform on pro-growth policies and delivering results for people; and in the international financial institutions, Treasury is advocating a sharper focus on measurable results, economic policy performance, and promoting private sector development.

Recent Economic Developments

The world economy has strengthened during the course of this year, and the United States is leading the way. Thanks to timely fiscal and monetary policy responses, economic growth in the United States is picking up now after the severe shocks of

the terrorist attacks, corporate accounting scandals, and stock market decline of 2000. Growth accelerated to 3.3 percent in the second quarter, with fixed investment as well as personal consumption posting large gains. The President's Jobs and Growth plan, along with low interest rates, put the U.S. economy in an excellent position to achieve sustained, robust growth. The President's six-point plan to enhance growth and job creation will further boost our performance. We will not be satisfied until we see strong and sustained job growth.

Looking beyond the United States, global growth is also improving. There are signs of stronger growth in Japan, as well as in the United Kingdom, Canada and several emerging market countries. Much of Europe, however, is still falling short of a strong economic recovery. While we can be pleased with the progress made, growth in the major economies around the world, as a whole, has been too slow for too long.

The U.S. International Accounts

From my discussions with my counterparts in other countries, there is a great appreciation worldwide that the U.S. is a force for strong growth. This strong performance is also reflected in the pattern of our external trade and current account balances.

Developments in the current account are best understood in terms of developments in investment and saving. As a matter of accounting, the current account deficit is equal to the gap between national investment and national saving. Thus, when investment in the United States is higher than domestic saving, foreign investors make up the difference, and the United States has a current account deficit.

Our current account deficit in large part reflects the attractive investment environment and high growth of productivity in the United States. Increased saving in the United States along with stronger growth abroad will reduce the deficit in the current account.

Exchange Rate Policies

The Report shows that countries around the world continue to follow a variety of exchange rate policies ranging from a flexible exchange rate regime with no or little intervention to currency unions and full dollarization. While the choice of an exchange rate regime is up to each country, we have been encouraging countries to use flexible exchange rates. Flexible exchange rates ease the adjustment to changing economic conditions in the international financial system. Of course, a flexible exchange rate will not prevent the economic damage that is caused by a bad economic policy. For example, even with a flexible exchange rate, an inflationary monetary policy would lead to a weak, constantly depreciating currency with negative effects on economic growth. A good flexible exchange rate regime requires a monetary policy with a focus on the goal of price stability, and has a transparent procedure for setting the policy instruments.

We are encouraging the use of flexible exchange rates with our major trading partners, we recognize that, especially in the case of small open economies, there are benefits from a "hard" exchange rate peg, such as dollarization, joining a currency union, or using a credible currency board. Of course, just as in the case of flexible exchange rates, a "hard" peg will not prevent the economic damage caused by a bad economic policy.

The G7 statement from Dubai, which I mentioned earlier in the context of the "G-7 Agenda for Growth," also addresses exchange rate policy. Here is what that statement said:
"We reaffirm that exchange rates should reflect economic fundamentals. We continue to monitor exchange markets closely and cooperate as appropriate. In this context, we emphasize that more flexibility in exchange rates is desirable for major countries or economic areas to promote smooth and widespread adjustments in the international financial system based on market mechanisms."

All G7 Ministers and Central Bank Governors—including Alan Greenspan and myself—agreed with that statement. And let me be clear: the G-7 message is

consistent with our strong dollar policy which I have consistently reiterated since my confirmation hearing. As I have said often, a country can not devalue itself into prosperity. A strong dollar is in the U.S. national interest. The G-7 message is also consistent with the Agenda for Growth, which is about a stronger world economy and flexibility.

Among the many currencies discussed in the Report, China's received special attention. China does not meet the technical requirements of the 1988 Trade Act -- the same finding for nearly ten years of past reports. China's global current account surplus has declined, and China has had a peg over a long time period during both upward and downward pressures on the currency. But it is clear that a flexible, market-based, exchange rate is appropriate for China. Given China's strong growth and substantial foreign exchange reserves, following on a series of economic reforms, China now has an opportunity to show leadership on the important global issue of exchange rate flexibility.

Greater exchange rate flexibility would allow China greater scope to maintain a low-inflation, pro-growth monetary policy. It would also enable China to enjoy the benefits, while helping mitigate the risks, of a more open capital account. And it would help improve the allocation of resources and the quality of financial intermediation in the Chinese economy. More broadly, a more flexible rate would help reduce macroeconomic imbalances.

A rules based system of trade and finance is essential for all nations to maximize the benefits of trade and generate the highest levels of economic growth. A pegged exchange rate is not appropriate for a major economy like China and should be changed.

For all these reasons, we are continuing our efforts to urge the Chinese to adopt a flexible exchange rate. I took this case to Beijing last month, emphasizing the need for exchange rate flexibility, along with reductions in barriers to trade and capital flows. And last weekend, following immediately on the heels of the President's meeting with President Hu, I met with the Chinese Finance Minister and Central Bank Governor in Mexico.
China's response to this engagement is encouraging:
• Earlier this month China's central bank governor said: "With the role of the market becoming increasingly important, the exchange rate of the RMB will be finally determined decisively by the market forces and have great flexibility."
• China's central bank is undertaking a number of capital market liberalization measures. In addition, Governor Zhou has endorsed a project in which the Chicago Mercantile Exchange and the Foreign Exchange Trade System & National Interbank Funding Center of China will develop a currency futures market in China.

• Vice Premier Huang Ju has accepted my invitation to come to Washington for an in-depth high-level discussion of these issues.

• A new technical cooperation agreement on financial issues related to exchange rates was announced by President Bush and President Hu. China's central bank governor and I will be responsible for implementing this program.

• The G-7 finance ministries and the Chinese finance ministry and central bank have begun talks on economic and financial market issues for the first time ever. Their first meeting was last month in Dubai.

We are encouraged by the steps the Chinese are taking, but we urge continued and speedy progress toward the goal of exchange rate flexibility. The Chinese are discussing exchange rate policy in international fora, and at home. China's leadership recently called for active advance of the reform in the financials system and exchange rate policy. The leadership also recognized that opening up of its capital market is seen by Beijing as an important step in moving to a flexible exchange rate. Further, the establishment of a strong regulator will help China's banking system see much needed improvement. Success will require daily engagement with the Chinese. For this reason, the Treasury Department is establishing an attaché presence in China.

As this example of China indicates, I recognize the need to address exchange rates

as part of our overall international economic strategy. But, as the example of China also indicates, I believe that the course we are on of financial diplomacy is the right course and the most effective way to bring about change.

Conclusion

Strengthening the economic recovery in the United States is our key economic objective. I am very concerned about job creation in the United States. The President's Six Point Plan is designed to remove impediments to growth and job creation. We have undertaken an ambitious drive to remove rigidities and barriers wherever they exist and to thereby create a level playing field that promotes increased international trade. The G-7 Agenda for Growth is an important step forward. So, too, are the bilateral discussions we have had with many countries on economic and financial issues. We will continue to work hard to accomplish our objectives.

Thank you.

Recently announced PRC capital market (and related) liberalization measures

• 2003: Simplification of rules concerning outward FDI.

• 2003: Agreement to allow IFIs to issue renminbi denominated bonds.

• 2003: Foreign banks allowed to begin buying Chinese securities under Qualified Foreign Institutional Investor scheme.

• 2003: Some Chinese firms allowed to retain 100% of foreign exchange earnings.

• 2003: China's first domestic issue of U.S. dollar bonds (by China Development Bank).

• 2003: Broader range of domestic assets owned by emigrants and non-residents allowed to be exchanged into foreign currency and repatriated.

• 2003: Multinational corporations allowed to consolidate foreign exchange transactions at national level.

• April 2003: New Chinese Bank Regulatory Commission established.

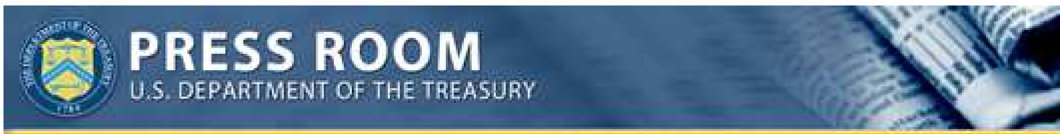
• October 2003: Limit raised on foreign currency allowed to Chinese travelers.

• October 2003: Regulations issued allowing non-bank institutions to provide auto financing.

• Subject to approval: Some insurance firms granted licenses to price premiums and benefits in foreign exchange.

• Subject to approval: Limit increased on foreign ownership share in Chinese banks.

• Subject to approval: Chinese insurance firms allowed to invest in foreign bonds.



FROM THE OFFICE OF PUBLIC AFFAIRS

October 30, 2003
JS-954

Report to Congress on
International Economic and Exchange Rate Policies
October 2003

This report reviews developments in international economic policy, including exchange rate policy, focusing on the first half of 2003. The report is required under the Omnibus Trade and Competitiveness Act of 1988, which states that "The Secretary of the Treasury shall analyze on an annual basis the exchange rate policies of foreign countries, in consultation with the International Monetary Fund, and consider whether countries manipulate the rate of exchange between their currency and the United States dollar for purposes of preventing effective balance of payments adjustments or gaining unfair competitive advantage in international trade."

After reviewing developments in the United States, the report examines exchange rate policies in major countries across five regions of the world: (1) the Americas, (2) Europe and Eurasia, (3) Africa, (4) the Middle East and South Asia, and (5) East Asia. To summarize, the report finds that

• Countries around the world continue to follow a variety of exchange rate policies, ranging from a flexible exchange rate with little or no intervention to currency unions and full dollarization. For example, Canada follows a flexible exchange rate regime with no intervention, Greece recently joined the European Monetary Union, and El Salvador maintained its dollarization regime.

• A notable trend observed over the past several years is the move by many countries to adopt flexible exchange rates, combined with clear price stability goals and a transparent system for adjusting monetary policy instruments. It is good news that nearly 100 countries have eschewed pegged exchange rates and have chosen to use a flexible exchange rate, dollarize, join a currency union, or create a currency board.

• The report finds that no major trading partner of the United States meets the technical requirements for designation under the Omnibus Trade and Competitiveness Act of 1988 during the first half of 2003. The report notes that while a number of countries continue to use pegged exchange rates and/or intervene in foreign exchange markets, a peg or intervention does not in and of itself satisfy the statutory test. Treasury has consulted with the IMF management and staff, as required by the statute, and they concur with our conclusions. The Administration strongly believes that a system of flexible, market-based exchange rates is best for major trading partners of the United States.

• For this reason, Treasury is continuing to engage actively with countries and to encourage, in both bilateral and multilateral discussions, policies that promote a flexible market-based exchange rate combined with a clear price stability goal and a transparent system for adjusting policy instruments. For example, one important accomplishment was the communiqué of the G7 Finance Ministers and Central Bank Governors in September of this year endorsing an Agenda for Growth and stating that "more flexibility in exchange rates is desirable for major countries or economic areas to promote smooth and widespread adjustments in the international financial system, based on market mechanisms."

The United States International Accounts

In assessing the trade deficits and surpluses of individual countries with the United States, it is important to examine first the overall U.S. trade and current account balance.

Saving, Investment, and the Current Account

Developments in the overall trade or current account balance are best understood in terms of developments in investment and saving. The current account deficit is conceptually equal to the gap between investment and saving as a matter of international accounting. When investment in the United States is higher than domestic saving, then foreigners make up the difference, and the United States has a current account deficit. In contrast, if savings exceed investments in a country, then that country has a current account surplus as its people invest abroad.

In the second quarter of 2003, for example, the U.S. current account deficit was $570 billion (at a seasonally adjusted annual rate and adjusted to a national income accounting basis) or 5.3 percent of GDP. This $570 billion deficit equaled the gap between $1,977 billion in investment and $1,407 billion in saving . That is, U.S. domestic investment was $570 billion more than domestic saving with net foreign investment making up the difference.

Viewed in these terms over the past year, the increase in the U.S. current account deficit was caused by an increase in investment, combined with a somewhat smaller decline in saving. Over the year ending in the second quarter of 2003 the current account deficit rose by $73 billion from the second quarter of 2002. During that same period investment rose by $40 billion and saving fell by $33 billion. The increase in investment reflected the acceleration in U.S. economic growth during 2003. Overall, real GDP grew at a 3.3 percent annual rate in the second quarter, up from 1.4 percent in the first quarter. Business investment in equipment and software investment posted large gains, and forward momentum in those sectors continued into the third quarter.

The current account was $555 billion in deficit on a balance of payments basis in the first half of 2003. How has the deficit been financed? The largest single part of financing the current account deficit has recently been net private foreign purchases of U.S. securities, which reached $436 billion in the first half of 2003. (Included in these were net foreign purchases of U.S Treasuries amounting to $151 billion.) In addition, foreign official institutions increased their U.S. assets by $197 billion. These items alone more than covered current account financing needs and the total of all other financing items were equal to a net $78 billion capital outflow.

Due to the current account deficit the net investment position of the United States (with direct investment valued at the current stock market value of owners' equity) fell to a negative $2.6 trillion at the end of 2002 from a negative $2.3 trillion at the end of 2001. Despite this large negative position, net income payments on investment assets were not significant in 2002, amounting to roughly $1 billion. These positive net income receipts are the result of large net inflows of income from direct investment offsetting net outflows of income on portfolio investment.

[Note: Balance of payments statistics are compiled on a slightly different basis than national income statistics. The net foreign investment (-$570 billion) item in the national income accounts closely matches the current account balance (-$555 billion) in the balance of payments. Saving includes the statistical discrepancy between the income and product accounts.]

The U.S. Dollar

According to the Federal Reserve Board's "broad" nominal dollar index, the U.S. dollar registered a 5.1 percent depreciation during 2003H1. The decline was 8.3 percent against "the major foreign currencies" (largely the industrialized countries) and 1.5 percent against "other important trading partners" (largely emerging market economies). The broad index declined 9.2 percent from February 27, 2002, when it reached its recent peak, through June 30, 2003.

Inflation remained subdued during this period. The consumer price index rose 2.1 percent over the 12 months ending in June as energy prices increased, while the

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core rate (excluding food and energy) increased 1.5 percent. The Federal Reserve maintained the federal funds rate target at 1.25 percent through the first five months of the year, then lowered the rate to 1.0 percent in June. During 2003H1, U.S. interest rates declined toward historical lows, and interest rate differentials increasingly favored relatively higher yielding non-dollar placements.

As discussed below, the currencies of different economies showed varying degrees of flexibility relative to the dollar, as some monetary authorities sought to dampen or prevent movements of their exchange rates against the dollar while others did not intervene at all. The United States did not intervene in foreign exchange markets during the first half of 2003.

The Americas

Overall, nominal exchange rates in the region appreciated or remained relatively stable relative to the U.S. dollar during the first half of 2003, with the Canadian dollar noticeably strengthening against the U.S. dollar. Interest rate spreads between the Latin American Emerging Market Bond Index (EMBI+) and U.S. Treasury securities continued to decline from the September 2002 high of 1366 basis points, ending June at 697 basis points above U.S. Treasuries.

A recovery appears to be emerging in many countries in Latin America following a disappointing year in 2002. The region saw real GDP decline 0.1 percent in 2002, but GDP is expected to grow 1.1 percent in 2003. Canada's GDP declined in the second quarter of 2003, but with stronger subsequent growth Canada is expected to achieve 2.0 percent growth for the year.

Canada

Canada's overall current account surplus rose to 2.0 percent of GDP in the first half of 2003, up from 1.7 percent in 2002H2, but still below the somewhat higher ratios recorded in 2000 and 2001. After little net change in 2002, the Canadian dollar rose 16.5 percent against the U.S. dollar between the end of 2002 and the end of June 2003, with the J.P. Morgan real trade-weighted Canadian dollar index up 11.4 percent over the period.

Canada has a flexible exchange rate and did not intervene in exchange markets during 2003H1. Canada has not intervened in foreign exchange markets since 1998, except to make a small contribution to the brief G-7 intervention in support of the euro in September 2000.

Argentina

Argentina has had a flexible exchange rate since the end of 2001 when it abandoned its convertibility law, which had pegged the peso one-to-one with the U.S. dollar. Argentina's currency continued to strengthen in the first half of 2003, moving from 3.36 pesos per dollar at end-December 2002 to 2.81 at end-June 2003 for a 19.6 percent appreciation. Argentina's trade surplus was $8.7 billion in the first half of 2003, with exports rising 16 percent and imports rising 38 percent compared with the same period the previous year. Argentina's gross foreign exchange reserves grew by $1.7 billion during the first half of the year to $12.2 billion at the end of June 2003. The economic recovery continued after the severe contraction in the first half of 2002, with real GDP growing 10 percent in the first quarter of 2003. Consumer prices were stable, with a net increase of 2.1 percent from end-December 2002 to end-June 2003, and conditions in the banking system continued to improve. Interest rates on saving deposits of 30-59 day maturities fell from over 20.7 percent at the beginning of 2003 to 9.6 percent by end-June 2003.

Mexico

Mexico has a flexible exchange rate. The Mexican peso depreciated 2.9 percent from 10.2 pesos per dollar at end-December 2002 to 10.5 pesos at end-June 2003, following an 11.2 percent depreciation in 2002. The real trade-weighted value of the peso depreciated 3.1 percent in the first half of the year, following a 3.6 percent depreciation last year. The current account deficit fell to 0.6 percent of GDP in the period, with seasonally adjusted imports falling 6.5 percent and exports increasing 4.7 percent compared with the second half of 2002. Foreign direct investment in

Mexico was $5.2 billion in the period, a decline of 26.4 percent from the comparable period last year. International reserves grew $4.6 billion over the period, reaching $55.2 billion by end-June. Economic conditions remain soft, with real GDP for the first half of 2003 growing at a 0.2 percent annual rate from the second half of 2002 and 1.2 percent from the comparable period last year.

Brazil

The real appreciated 22 percent in the first half of 2003. Brazil registered a current account surplus of $535 million for the first half of the year, driven by a $10.4 billion trade surplus. This performance compares with an $8.4 billion current account deficit for the first half of 2002. Net international reserves increased from year-end 2002 by $400 million to $14.6 billion at the end of June, while gross international reserves totaled $48.0 billion, up from $38.7 billion at 2002 year-end. (IMF disbursements are not included in the calculation of net reserves.)

Consumer price inflation was 17 percent for the twelve months ending in June 2003. In this environment, the central bank tightened monetary policy in January and February, raising the target monetary policy interest rate 150 basis points to 26.5 percent. The central bank began to ease monetary policy in June with a 50 basis point cut following declining inflation readings in May and June.

Europe and Eurasia

In the European Monetary Union, the euro appreciated strongly against the dollar, and in Russia, oil sales and an improved capital account supported the ruble. In Central Europe, weakness in the major economies led to weakness against their key trading currency, the euro.

The European Monetary Union

The countries in the European Monetary Union as a whole had a current account surplus during the first half of 2003 equal to $14 billion. Goods exports fell 3.8 percent in the first half of 2003 from the second half of 2002, and goods imports increased by a mere 0.8 percent. The current account surplus for 2003H1 was down 60.1 percent from that of 2002H2 (in dollar terms). The underlying movement behind this change appears to have been an increase in investment and a decline in saving in the Euro-zone. Gross capital formation (seasonally-adjusted) grew by 1.4 percent between the two time periods. Saving is estimated to have fallen 1.6 percent between 2002H2 and 2003H1.

The financial account for the Euro-zone was dominated in 2003H1 by a large deficit in “other investment” of $124.6 billion, down 15.2 percent from $146.9 billion in 2002H2. The biggest contributors to “other investment” were short-term loans by monetary financial institutions and loans from other sectors. There were smaller deficits in financial derivatives (- $5.1 billion) and direct investment (- $4.5 billion). The Euro-zone saw surpluses in portfolio investment ($36.5 billion, down 48.8 percent from 2002H2) and accumulation of reserve assets of $16.2 billion (compared to a fall in reserves of $5.9 billion in 2002H2).

The euro appreciated 9.7 percent against the dollar in the first half of 2003, while according to the Eurostat index the real effective exchange rate appreciated 8.4 percent. The European Central Bank did not intervene in exchange markets during this period.

Russia

In the first half of 2003, Russia saw large net inflows of foreign exchange resulting from high oil prices and high foreign borrowing by Russian corporations. This led to a 5.3 percent appreciation of the ruble against the U.S. dollar compared to a 1.3 percent depreciation during the second half of 2002. Intervention by the Russian monetary authorities to moderate the appreciation of the ruble against the dollar led to a $16.6 billion increase in foreign exchange reserves to a record high of $64.4 billion.

Central Europe

After appreciating steadily for several years in real terms, the currencies of the major Central European economies began to show weakness in both nominal and real terms during 2003H1. Nominal depreciation of key regional currencies against the euro, the most important foreign currency for trade, combined with a slowdown in inflation in the major area economies to reverse the real appreciation trend.

In Poland, for example, the zloty weakened in both nominal terms (1.9 percent versus the dollar and 10.5 percent versus the euro) and real terms during the period as the fiscal deficit grew and confidence in the zloty faltered. The Czech Republic koruna depreciated in real terms due to deflation during the period and political uncertainty. In Hungary the forint saw extreme volatility against the euro. A strong appreciation in the beginning of the year prompted massive intervention by the central bank of Hungary. However, deteriorating macroeconomic conditions and market uncertainty concerning the course of fiscal reform led to capital flight and depreciation. The Bulgarian lev appreciated against the dollar as its value was fixed relative to the euro as part of its successful currency board arrangement.

Africa

Most key exchange rates in Africa depreciated against the U.S. dollar on a nominal basis during the first half of 2003. Notable exceptions were the South African rand, which appreciated 14.7 percent, and the currencies of the CFA zone, which are pegged to the euro. They appreciated against the dollar just as the euro did. The strengthening of the rand probably reflected favorable interest rate differentials, improved investor sentiment following credit ratings upgrades, and the country's more sound economic fundamentals.

GDP growth in Africa remained resilient despite the weak pace of recovery in industrialized countries. For the continent as a whole, growth is expected to increase in 2003. The continent's overall current account deficit is expected to fall slightly in 2003 from 1.3 percent of GDP in 2002, though current account deficits in many countries in sub-Saharan Africa remain relatively high. Capital inflows are expected to increase, particularly from private sources. Since 2001, foreign exchange reserves have increased from $64.7 billion to a projected $86.7 billion in 2003, with the bulk of the reserve accumulation occurring in North African countries due to higher energy prices.

In Egypt the Egyptian pound is notionally floating but strongly managed. The pound did move substantially over the period, however, falling 23 percent against the dollar and 25 percent on a real trade-weighted basis. The current account surplus grew during the first half of 2003, reaching 1.5 percent of GDP in the second quarter compared to 0.4 percent in the same quarter the year before, due in part to a slight contraction in imports but more significantly to an increase in both oil and non-oil exports.

Middle East and South Asia

The Middle East has seen strong growth this year, largely fueled by high global oil prices. Regional growth in 2003 should end up greater than last year's 3.9 percent, with the growth largely centered in the oil-exporting countries.

Many countries in this region maintain inflexible exchange rate regimes, including narrow bands and explicit or implicit pegs to the dollar. The high price of oil has led to higher current account surpluses and official reserve accumulation among the oil exporters. In Saudi Arabia, for example, reserves increased 12 percent in the first four months of this year to reach $23.1 billion, the highest level in a decade. The current account surplus is expected to increase well above the 6.2 percent of GDP level in 2002. Among the non-oil exporting countries, the current account deficit is expected to widen in 2003 from the 0.5 percent of GDP deficit recorded in 2002. In addition to higher oil prices, these countries were also hit by declines in tourism revenues due to the uncertainty surrounding the conflict in Iraq.

India maintains a heavily managed exchange rate regime. While the rupee appreciated 3.4 percent against the dollar in the first half of 2003, the Indian authorities intervened to limit further appreciation. As a result, foreign reserves

grew $11.6 billion in the first half of the year, reaching $78 billion by end-June. The current account returned to a small deficit (seasonally adjusted) after surpluses in 2002. Capital inflows, including FDI, increased due to the improved economic outlook and expectations of an appreciation of the rupee.

Turkey and Israel have flexible exchange rates. Both currencies appreciated significantly since the start of the year, buoyed by strong investor demand for emerging market assets. The Turkish lira appreciated 18.3 percent between the end of December 2002 and the end of June 2003, following a 12.7 percent depreciation in 2002. The current account deficit fell to 1.6 percent of GDP in the first 6 months of 2003 from 3.0 percent of GDP in the second half of 2002. Gross foreign exchange reserves grew $2.1 billion over the period, reaching $28.8 billion by end-June.

Similarly the new Israeli shekel appreciated 9.8 percent from end-December 2002 to end-June 2003, following a 7.3 percent depreciation in 2002. The current account balance grew to a 1.8 percent of GDP surplus in the period, compared to a 1.0 percent deficit in 2002. Foreign exchange reserves grew 2.0 percent over the period, reaching $24.6 billion by end-June.

East Asia

Asian currencies were generally stable against the dollar in the first half of 2003, although the Indonesian rupiah and Thai baht both appreciated near the end of the period. Currency stability was maintained against the backdrop of a high degree of regional economic uncertainty, stemming from SARS and oil prices. Uncertainties regarding the oil price outlook were reduced after the start of the military campaign in Iraq. Efforts to contain SARS proved successful, and its economic effect, while significant for some countries, was less than anticipated.

Japan

Japan's current account surplus grew to $62 billion (3.0 percent of GDP) in the first half of 2003, up from $54 billion (2.6 percent of GDP) in the second half of 2002. While Japan's merchandise trade surplus declined by 9 percent during the period to $45.2 billion, Japan's services deficit narrowed substantially to $15.4 billion, 35 percent smaller than in the second half of 2002. Japan had a bilateral merchandise trade surplus with the United States of $32.2 billion during 2003H1, down from $36.8 billion in 2002H2, and from $33.1 billion in 2002H1.

The persistent Japanese global current account surplus reflects the high rate of Japanese domestic saving relative to domestic investment. The trend rate of Japanese growth fell after the first oil crisis, and again after the bursting of Japan's asset price bubble at the beginning of the 1990's. Slower growth has meant lower investment, and the share of private investment in GDP has fallen from 26 percent in the 1960's, to 22 percent in the 1980's, to 19 percent in the last 3 years. Excess private saving has been partially absorbed by larger government deficits.

During the first half of 2003, the yen fluctuated in a narrow range against the dollar, depreciating 0.9 percent to ¥119.9 at the end of June 2003 from ¥118.8 at the end of December 2002. But in September and October of this year the yen appreciated against the dollar to around the 108 level or about 7 percent since the beginning of September. Intervention by the Japanese monetary authorities in the exchange markets totaled $59.0 billion in the first half of 2003 and continued in July and August with an additional $22.7 billion. Japan's foreign exchange reserves grew by 17 percent to $527 billion at the end of June, up from $451 billion at the end of December 2002. Taking the longer view over the past 3 years it has fluctuated between a low of 135 and a high of 108. The Japanese have stated that their "intervention is carried out when excess volatility or over-shooting is observed in the markets." The Treasury is actively engaged with the Japanese on these issues both bilaterally and through the meetings of the G7 finance ministry and central bank officials.

China

China's overall trade surplus narrowed in the first half of 2003 to $13.5 billion (2.2 percent of GDP), compared to $20.7 billion a year earlier (3.8 percent of GDP). The

reduced overall trade surplus was accounted for by the strong growth in China's merchandise imports compared to exports. This reflected China's growing deficit with trading partners other than the United States. Other Asian economies that used to export directly to the United States increasingly ship components to China for assembly. China's bilateral surplus on trade in goods with the United States grew to $53.9 billion in 2003H1, up from $43.1 billion a year earlier.

China's current account surplus in 2003H1 was $11.1 billion compared to $13.6 billion in 2002H1. However, net FDI inflows were $26.9 billion, while non-FDI net capital inflows were $17.5 billion, compared to $22.7 billion and -$10.4 billion a year earlier, respectively. Thus, the increase in China' official reserves was due more to capital inflows than to the much smaller current account surplus.

China has pegged its currency since 1994 at 8.28 to the dollar. This policy is not appropriate for a major economy like China and should be changed. The Administration has engaged in direct talks calling on the Chinese to move towards a flexible exchange regime. The Administration has utilized bilateral and multilateral forums to urge China to move toward greater flexibility. At the September 2003 G7 meeting in Dubai, the ministers and central bank governors endorsed flexibility in exchange rates for large economies. Secretary Snow traveled to China for discussions with senior Chinese officials on financial issues including exchange rate policy. President Bush, in his bilateral meeting with President Hu, discussed China's exchange rate policy.

China has maintained its fixed exchange rate despite significant changes – up and down – in the exchange rate of the dollar vis-à-vis other currencies. Recently there has been strong pressure on the yuan, as evidenced by foreign exchange reserves rising to $346 billion in June 2003, up 43 percent from June 2002. The Chinese government has indicated that it will move to a flexible exchange rate regime. It is taking steps to get there and the U.S. is providing technical cooperation. However, it also has stated that doing so immediately would harm the banking system and the overall Chinese economy.

In his discussions, Secretary Snow stressed the desirability of China's moving to a flexible market-based exchange rate regime and reducing controls on capital flows. The Chinese economy is now one of the largest in the world, and China is a major player in world trade. The Chinese capital account is expected to become increasingly open, and policies of maintaining a currency peg in the face of an increasingly open capital account increases risk. Greater exchange rate flexibility would also allow China greater scope to maintain a low-inflation, pro-growth monetary policy. It would improve the allocation of resources and the quality of financial intermediation in the Chinese economy. Moreover, such a change would be consistent with our view that the international trading system works best with free trade, the free flow of capital and with market-based exchange rates.

Serious engagement with China on these issues will continue. A new Technical Cooperation Program is being implemented under the leadership of the Secretary of the Treasury and the Governor of the central bank of China. This program can help create the market mechanisms needed to make the transition to a flexible exchange rate regime. Moreover, the Chinese deputy finance minister and deputy central bank governor have begun to have regular meetings with the G7 finance deputies, with the first meeting held in Dubai in September and the next one scheduled for Paris in November.

Korea

Korea entered its first recession in five years during the first half of 2003. Real GDP contracted 2.9 percent in the second quarter of 2003, continuing the 1.6 percent drop in the first quarter. The slowdown was due to contracting domestic demand combined with slowing external sales. In response, both fiscal policy and monetary policy have been eased. In July the overnight call rate was cut a quarter-point to 3.75 percent.

Korea's current account surplus for the first half of 2003 was $1.2 billion, down from $3.9 billion for the same period last year. The balance on capital and financial account transactions recorded an almost $3.0 billion increase as the result of

portfolio and other investment inflows. Official foreign reserves increased by $10.2 billion to $131.7 billion. The U.S. bilateral trade deficit with Korea in the first half of 2003 was $5.4 billion.

The won depreciated a net 0.8 percent in the first half of 2003 but has been on a rising path for several months. JP Morgan's real trade-weighted index of the won fell 2.3 percent during the period. While Korea has officially adopted a flexible exchange rate policy, in practice the won is quite closely linked to the Japanese yen. Since 2000 the monthly nominal won/yen exchange rate has averaged 1031, and the rate has deviated no more than 6 percent from this average.

Taiwan

After decreasing 2.4 percent in the first quarter of 2003, Taiwan's real GDP declined by a sharp 9.9 percent in the second quarter of 2003, reflecting the drag of SARS on the economy. Deflation remained entrenched, with consumer prices falling 2.2 percent in 2002 and 0.9 percent in the first half of 2003. Taiwan recorded a current account surplus of about 10.6 percent of GDP or $14.7 billion during the first half of 2003. The current account surplus was due mainly to a large, $13.4 billion, trade surplus with China and growing foreign investment earnings. The United States ran a $7.3 billion bilateral trade deficit with Taiwan in the first half of 2003.

Net portfolio investment recorded an extraordinary deficit of 20 percent of GDP during the first half of 2003, as residents' portfolio investment abroad increased 160 percent compared with the same period in 2002. These portfolio outflows were largely offset by other investment inflows, and the financial account recorded a more moderate deficit of 5 percent of GDP in the first half of 2003. In the first half of 2003, the new Taiwan dollar appreciated slightly (0.3 percent) against the U.S. dollar and also depreciated 4.3 percent on a real trade weighted basis, as measured by the JP Morgan index. Reserves increased by $15 billion during the first half of 2003. Taiwan's $177 billion in reserves are equivalent to almost 10 times its short-term external debt and almost twice the country's total foreign liabilities.

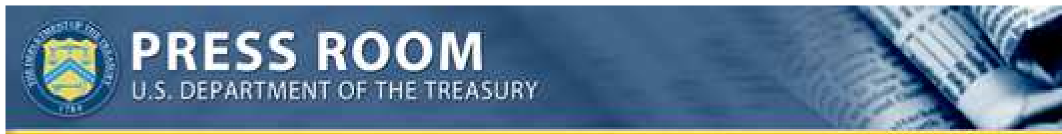
Taiwan is in the process of liberalizing its capital account regime; this liberalization has already resulted in a significant increase of flows in the financial account. The increase in outward portfolio investment over the last 18 months has eased appreciation pressures and reserve accumulation.

Malaysia

After a strong rebound in 2002, Malaysia's economy slowed in the first half of 2003. Real GDP grew 3.0 percent in the first quarter and 6.1 percent in the second quarter. The current account surplus increased to 12.3 percent of GDP in the first half of 2002 from 7.2 percent a year earlier, reflecting slowing domestic demand growth. Malaysia's bilateral trade surplus with the United States increased to $6.6 billion in 2003H1 from $6.0 billion in 2002H1.

Malaysia has maintained a fixed peg to the dollar since September 1998, when it also imposed capital controls. Controls on capital flows have since been relaxed, but offshore trading of the ringgit remains prohibited and foreign portfolio investment by residents continues to be restricted. The ringgit depreciated 2.7 percent over the period on a real trade-weighted basis, according to the JP Morgan index. At the end of June, reserves stood at $36.8 billion, up from $34.2 billion at end-2002.

Penolakan China..., Eflina Pehulita Sinulingga, FISIP UI, 2008



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May 19, 2005
JS-2459

Treasury Secretary Snow Appoints Olin L. Wethington as Special Envoy on China

Treasury Secretary John Snow today announced that he is appointing Olin L. Wethington as his Special Envoy on China. Mr. Wethington will be responsible for direct engagement with China on issues related to exchange rate and financial market reform.

"I'm very pleased that Olin Wethington has agreed to take on this assignment," said Secretary John Snow. "His appointment comes at a time when continuation of certain policies constrains adjustment of international imbalances and poses risk to global economic growth. His appointment seeks to continue and intensify a constructive dialogue with China on these issues. This is a critical time for China to implement necessary economic reforms – most notably, reform of its currency regime and the adoption of market-based exchange policies. Olin Wethington brings extensive experience and talent to this position. I have enormous confidence in his ability to do this job."

Secretary Snow directed Mr. Wethington, in carrying out his responsibilities, to consult with other governments as necessary, particularly in Asia and among the G-7, and with international financial institutions, most importantly the International Monetary Fund.

His responsibilities will also include the China portfolio of Ambassador Paul Speltz, who will continue his full-time position as U.S. Executive Director at the Asian Development Bank in Manilla, Philippines. Secretary Snow praised the work of Ambassador Speltz: "Ambassador Speltz did an outstanding job over the past year and has achieved so much, particularly with our Technical Cooperation Program with China. There is no greater testament to Paul's accomplishments than the fact that China today is now ready to introduce currency flexibility. I greatly appreciate the job he has done and I am very pleased that he will continue to represent the United States at the Asian Development Bank."

"It is a great honor to take this assignment, as it is an important priority for the Bush Administration that China implements sound economic policies. I look forward to working with the Chinese government, as well as other governments in the region, and our partners in the G7 to encourage China to reform its currency policy. Such a reform is in China's best interest and it is in the best interest of the global economy," Wethington said.

Mr. Wethington has a successful track record in international financial diplomacy and deep experience in dealing with foreign governments on matters of financial market reform. In 1991-92, he served as Assistant Secretary for International Affairs at the U.S. Treasury. In that capacity, he led a number of important financial market initiatives, particularly in Asia, including the U.S./Japan Structural Impediments Initiative, and was a key participant in the dollar/yen talks. He also chaired the U.S./Korea financial services talks and led, on behalf of the Treasury, discussions during that period with China on exchange rate matters. He served as chief negotiator of the financial services components of the NAFTA, including banking, securities and insurance. In 1990-91, Mr. Wethington served as Executive Secretary, Economic Policy Council, at the White House. In the private sector, as a senior partner with Steptoe & Johnson LLP, he advised over the past several decades numerous major American companies on international financial and trade matters, including with respect to China.

More recently, Mr. Wethington served as Director, Economic Policy, with the Coalition Provisional Authority in Baghdad, where for close to eight months he was the senior Treasury official on banking, finance and economic matters, including the effort to build the capacity of the Central Bank and Finance Ministry of Iraq. Upon his return from Baghdad, he was named Counselor to the Secretary of the Treasury and played a central role in the international effort to reduce substantially Iraq's $125 billion external debt. He led the on-ground negotiations for the United States within the Paris Club that produced international agreement to eliminate 80% of Iraq's external debt--the largest debt write-down by sovereign creditors in the fifty-year history of the Paris Club.

Mr. Wethington will continue to serve in his capacity as Counselor to the Treasury Secretary.

He is a graduate of the University of Pennsylvania, where he majored in Oriental Studies, including Chinese history and language, and of the Harvard Law School.

REPORTS

- Snow Letter
- Speltz Letter

July 21, 2005
JS-2648

Statement by Secretary Snow on Reform of China's Currency

I welcome China's announcement today that it is adopting a more flexible exchange rate regime.

As we have said, reform of China's currency regime is important for China and the international financial system.

I particularly noted China's objective of allowing the market to fully play its role in resource allocation as well as "to put in place and further strengthen the managed floating exchange regime based on market supply and demand."

We will monitor China's managed float as their exchange rate moves to alignment with underlying market conditions.

China's full implementation of its new currency regime will be a significant contribution toward global financial stability.

The international economy performs best with free trade, the free flow of capital, and flexible currencies.

-30-

Penolakan China..., Eflina Pehulita Sinulingga, FISIP UI, 2008