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## FACT OF THE WEEK (January 26, 2010)

### CHINA'S RECORD RESERVES

Theory teaches that in a free currency market exchange rates will rise enough to reduce and eventually reverse the build-up of excessive official exchange reserves. In the case of China since 2005, nothing could be farther from the truth. From already high levels five or six years ago, China's reserves have risen relentlessly to a record \$2.4 trillion dollars. The attached graph and tables provide the startling statistics both for the People's Republic of China and the combined Chinese total including Hong Kong and Macau.

This is Exhibit A in the case for China's contribution to global imbalances. What they demonstrate is:

- The 2.1 percent revaluation of the renminbi (RMB) in July 2005 and the further 17.5 percent appreciation over the next 36 months did little to slow the accumulation of foreign exchange reserves in China. The change was too small and too gradual even to begin the process of reversing China's current account surplus with the world.
- In the six quarters since the RMB was effectively re-pegged to the dollar in July 2008, official reserves have risen even more rapidly than before. China reports a net increase of \$590 billion, or almost one third, in that span. China likes to claim credit for the "stability" of the RMB exchange rate. In fact, the new peg has had destabilizing effects, as reflected in the accelerating run-up in reserves at a time of global recession.
- Overall, China's reserves have more than tripled since the summer of 2005 to a level never even approached by any other country.
- It must be stressed that the reserves are *net* of China's massive purchases of raw materials, energy deposits and technology from all around the world.
- Moreover, the official reserves probably understate the full extent of hard currencies at China's disposal. When the official reserves of Hong Kong and Macao are included, China's acknowledged reserves approach \$2.7 trillion. Hong Kong, in particular, has been amassing additional reserves at unprecedented levels and now ranks seventh in the world, ahead of Brazil and Germany. On a per capita basis, each Hong Kong inhabitant is

backed by \$36,343 in reserves. To match that ratio, Mainland China would need more than \$7 trillion!

- In addition to the official reserves, China commands hundreds of billions of dollars worth of hard currency assets held by the sovereign wealth fund (soon to have \$400 billion), the social security investment fund, government-owned investment companies, commercial bank reserves, and corporate and individual accounts. It's likely that the total easily exceeds \$3 trillion – and it increases daily.

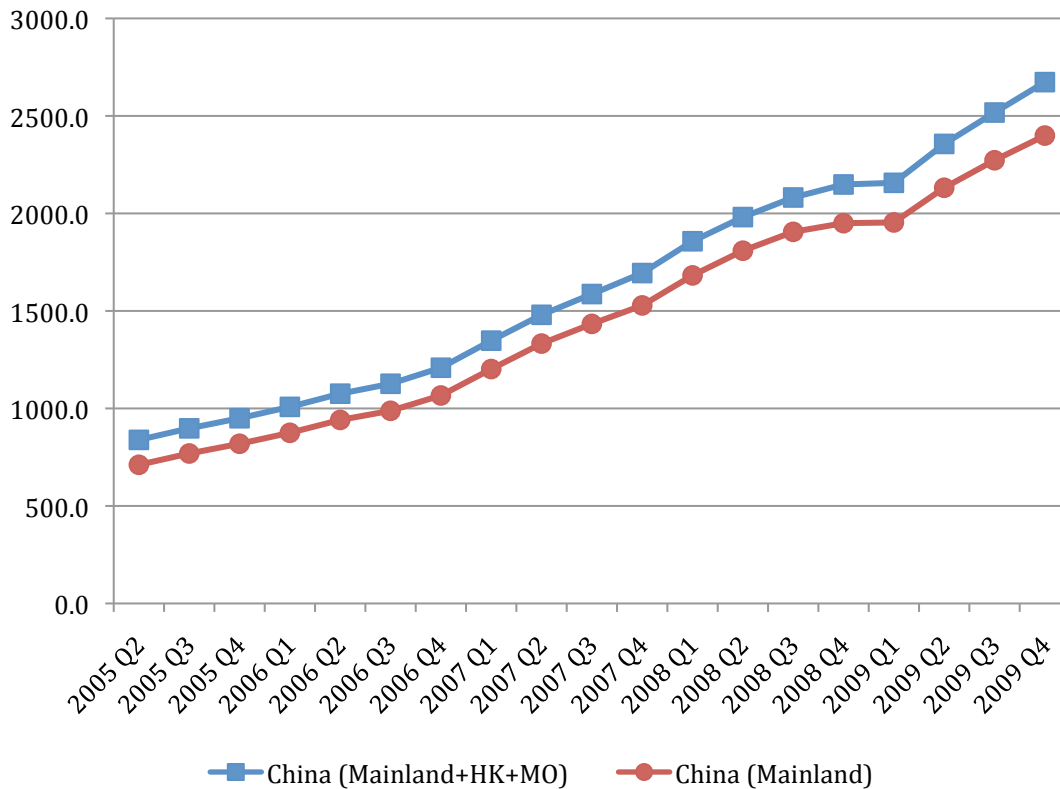
The bottom line, as Robert Samuelson wrote in a recent column, “China’s \$2.4 Trillion Grip on the Global Economy,” is:

The artificially depressed RMB hurts exports from developing countries and not just the United States, Europe and Japan. China grows at others' expense. The manipulation of trade subverts support elsewhere for open trading policies. For now, China has no desire to substitute the RMB for the dollar as the primary global currency. Its ambition is more sweeping: to create a world economy that serves China's interests and, only as an afterthought, anyone else's.

It's time to confront this problem before it ruins us all. The Congress can help by passing The Currency Reform for Fair Trade Act, H.R. 2378 and S. 1027, the only WTO-consistent legislation that addresses the subsidy effects of currency undervaluation.

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**Chinese Foreign Exchange Reserves**  
(Billions of USD)  
2005 Q2-2009 Q4



	2005 Q2	2005 Q3	2005 Q4	2006 Q1	2006 Q2	2006 Q3	2006 Q4	2007 Q1	2007 Q2
<b>China</b>	<b>838.7</b>	<b>897.9</b>	<b>949.8</b>	<b>1008.0</b>	<b>1075.6</b>	<b>1126.5</b>	<b>1208.7</b>	<b>1347.6</b>	<b>1480.1</b>
<b>Mainland</b>	711.0	769.0	818.9	875.1	941.1	987.9	1066.3	1202.0	1332.6
<b>Hong Kong</b>	122.0	122.7	124.3	125.8	126.6	130.3	133.2	135.4	136.3
<b>Macao</b>	5.7	6.2	6.7	7.1	7.9	8.3	9.1	10.2	11.1

	2007 Q3	2007 Q4	2008 Q1	2008 Q2	2008 Q3	2008 Q4	2009 Q1	2009 Q2	2009 Q3	2009 Q4
<b>China</b>	<b>1586.6</b>	<b>1694.2</b>	<b>1857.3</b>	<b>1981.2</b>	<b>2081.7</b>	<b>2148.4</b>	<b>2156.9</b>	<b>2356.4</b>	<b>2517.3</b>	<b>2673.3</b>
<b>Mainland</b>	1433.6	1528.2	1682.2	1808.8	1905.6	1950.0	1953.7	2131.6	2272.6	2399.2
<b>Hong Kong</b>	140.9	152.7	160.8	157.6	160.6	182.5	186.3	207.0	226.9	255.8
<b>Macao</b>	12.1	13.2	14.3	14.7	15.6	15.9	16.8	17.8	17.8	18.3

Sources: People's Bank of China; Monetary Authority of Hong Kong; Monetary Authority of Macao

## Foreign Exchange Reserves: Top Ten Countries

		Billions Of USD	At End Of
(1)	Mainland China	2,399.0	Dec 2009
(2)	Japan	1,049.4	Dec 2009
(3)	Russia	439.0	Dec 2009
(4)	Taiwan	348.2	Dec 2009
(5)	India	283.5	Dec 2009
(6)	Korea	270.0	Dec 2009
(7)	Hong Kong	255.8	Dec 2009
(8)	Brazil	238.5	Dec 2009
(9)	Germany	189.5	Nov 2009
(10)	Singapore	187.8	Dec 2009

Sources: International Monetary Fund; People's Bank of China; other central banks and monetary authorities, etc.