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China, Japan, America

By PAUL KRUGMAN

Last week Japan's minister of finance declared that he and his colleagues wanted a discussion with China about the latter's purchases of Japanese bonds, to "examine its intention" — diplomat-speak for "Stop it right now." The news made me want to bang my head against the wall in frustration.

You see, senior American policy figures have repeatedly balked at doing anything about Chinese currency manipulation, at least in part out of fear that the Chinese would stop buying our bonds. Yet in the current environment, Chinese purchases of our bonds don't help us — they hurt us. The Japanese understand that. Why don't we?

Some background: If discussion of Chinese currency policy seems confusing, it's only because many people don't want to face up to the stark, simple reality — namely, that China is deliberately keeping its currency artificially weak.

The consequences of this policy are also stark and simple: in effect, China is taxing imports while subsidizing exports, feeding a huge trade surplus. You may see claims that China's trade surplus has nothing to do with its currency policy; if so, that would be a first in world economic history. An undervalued currency always promotes trade surpluses, and China is no different.

And in a depressed world economy, any country running an artificial trade surplus is depriving other nations of much-needed sales and jobs. Again, anyone who asserts otherwise is claiming that China is somehow exempt from the economic logic that has always applied to everyone else.

So what should we be doing? U.S. officials have tried to reason with their Chinese counterparts, arguing that a stronger currency would be in China's own interest. They're right about that: an undervalued currency promotes inflation, erodes the real wages of Chinese workers and squanders Chinese resources. But while currency manipulation is bad for China as a whole, it's good for politically influential Chinese companies — many of them state-owned. And so the currency manipulation goes on.

Time and again, U.S. officials have announced progress on the currency issue; each time, it turns out that they've been had. Back in June, Timothy Geithner, the Treasury secretary, praised China's announcement that it would move to a more flexible exchange rate. Since then, the renminbi has risen a grand total of 1, that's right, 1 percent against the dollar — with much of the rise taking place in just the past few days, ahead of planned Congressional hearings on the currency issue. And since the dollar has fallen against other major currencies, China's artificial cost advantage has actually increased.

Clearly, nothing will happen until or unless the United States shows that it's willing to do what it normally does when another country subsidizes its exports: impose a temporary tariff that offsets the subsidy. So why has such action never been on the table?

One answer, as I've already suggested, is fear of what would happen if the Chinese stopped buying American bonds. But this fear is completely misplaced: in a world awash with excess savings, we don't need China's money — especially because the Federal Reserve could and should buy up any bonds the Chinese sell.

It's true that the dollar would fall if China decided to dump some American holdings. But this would actually help the U.S. economy, making our exports more competitive. Ask the Japanese, who want China to stop buying their bonds because those purchases are driving up the yen.

Aside from unjustified financial fears, there's a more sinister cause of U.S. passivity: business fear of Chinese retaliation.

Consider a related issue: the clearly illegal subsidies China provides to its clean-energy industry. These subsidies should have led to a formal complaint from American businesses; in fact, the only organization willing to file a complaint was the steelworkers union. Why? As The Times reported, "multinational companies and trade associations in the clean energy business, as in many other industries, have been wary of filing trade cases, fearing Chinese officials' reputation for retaliating against joint ventures in their country and potentially denying market access to any company that takes sides against China."

Similar intimidation has surely helped discourage action on the currency front. So this is a good time to remember that what's good for multinational companies is often bad for America, especially its workers.

So here's the question: Will U.S. policy makers let themselves be spooked by financial phantoms and bullied by business intimidation? Will they continue to do nothing in the face of policies that benefit Chinese special interests at the expense of both Chinese and American workers? Or will they finally, finally act? Stay tuned.

Ross Douthat is off today.