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GLOBAL SUPPLY CHAIN FOCUS

Global Supply Chain: One Call in China to Let Yaun Rise 10% Against Dollar

What would be the impact on China sourcing?

SCDigest Editorial Staff

A leading Chinese economist this week suggested that China should do a one-time appreciation of its yuan currency of 10% against the dollar, but whether this was a independent opinion or part of a coordinated government move to eventually enact such a change is unclear.

If such a move were to happen, it would effectively increase the price of Chinese imports to the US by 10%, in some cases eliminating the savings attained from offshoring there. However, suppliers in China could reduce prices to offset the currency swing, perhaps aided by government subsidies.

Zhang Bin, a research fellow at The Chinese Academy of Social Sciences, recently published a research paper that said "There is an urgent need" for reforming China's currency policy, and that now was the best time to do so.

He calls for a one-time adjustment of up to 10% in the value of the yuan versus the US dollar.

Unlike most major currencies, the yuan does not trade or "float" in global currency markets to set its value versus the dollar. Instead, the government sets the exchange rate of the yuan against the dollar, enabling the government to control the impact of currency on Chinese exports.

Last year, despite an up and down story for the dollar against most other major currencies, the yuan remained steady throughout 2009 against the greenback.

Many US government and labor leaders and some business interests have been very critical over the yuan policy in recent years. President Obama himself made some statements mildly critical of China's yuan valuation in late 2009. Critics argue that by keeping the yuan artificially low, it gives Chinese manufacturers an advantage over producers in the US, accelerates the rate of "offshoring," and contributes to the massive trade imbalance the US has with China.

Those criticisms have become louder under a Democratic Congress and administration, and may become more strident in 2010 as the economy continues to struggle and November elections approach.

Similar criticisms are coming from Europe.

In some cases, the Academy presents views that are in the end supportive of Chinese government plans, perhaps in a coordinated way. The paper from Zhang, however, runs counter to the official stance of the Chinese government now, which has long maintained its yuan policy is just fine.

Though the Chinese economy was said to grow over 8% in 2009, much of that came from the government's massive stimulus plan and infrastructure spending. Exports, the engine of the Chinese economy for the past decade, took a beating as the economies of the developed countries went through the worst recession in decades. Tens of thousands of Chinese factories shut their doors and millions of Chinese lost their jobs, many of them heading back to the countryside from more urban areas.

An appreciation of the yuan likely would hurt exports and perhaps cause more manufacturing job losses at least in the short term - something the government is very wary of, fearing social unrest.

Still, Zhang called for a "more reasonable" exchange rate, including the one time 10% appreciation followed by the ability of the yuan to float in a modest band of plus or minus 3% against the dollar annually.

While recognizing a yuan appreciation could bring some short term pain to exports and manufacturing jobs, Zhang wrote that "The dollar is no longer a good anchor point as pegging to the dollar would intensify fluctuations in domestic consumer prices and macroeconomic operations," probably referring to Chinese fears over the level of US government debt and increase in the amount of dollars being put into the economy by the Federal Reserve, each of which could decrease the value of the dollar over time.

This is a development global sourcing managers and supply chain leaders should keep tabs on.

Do you think the yaun needs to be re-valued against the dollar? Is this likely to happen? Would a 10% rise have much of an impact on US imports from China? Let us know your thoughts at the Feedback button below.

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