Comments on Professor Yu's Paper

The Global Financial Crisis and China's Policy Responses

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Global imbalance and the RMB issue

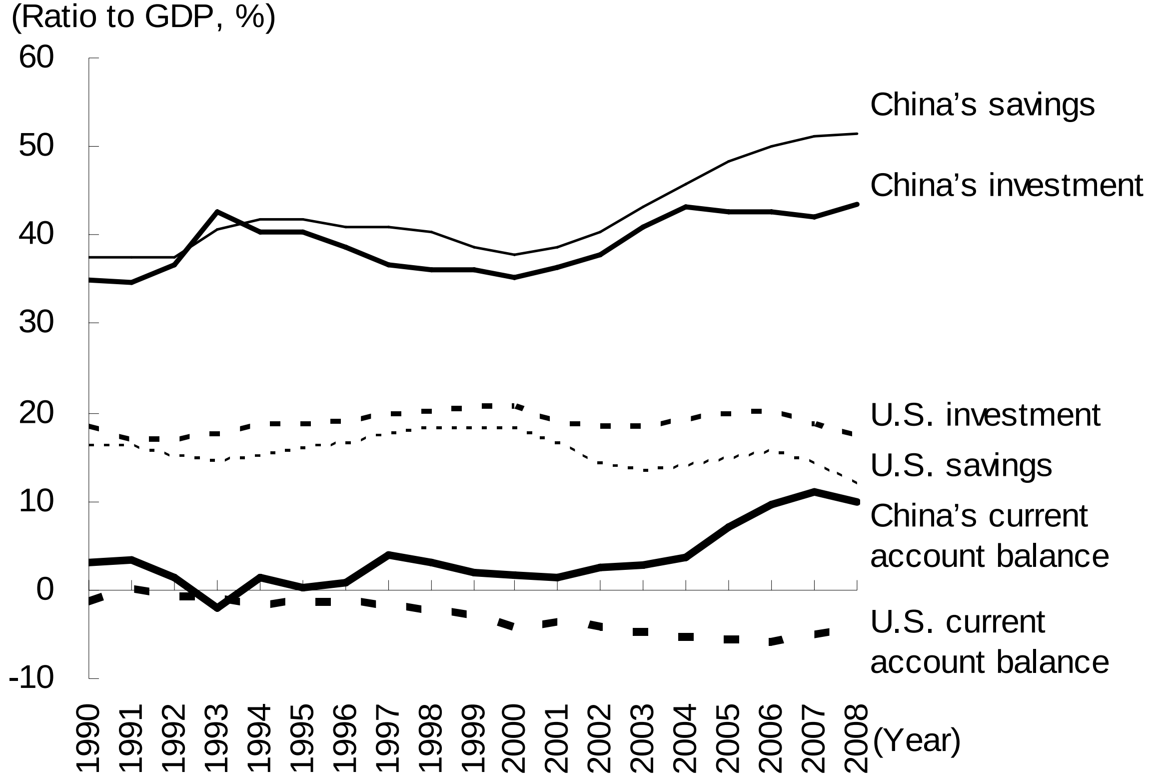
How to reduce the current account surplus

- Current account as the gap between savings and investment
- Raising consumption as the key to reduce current account surplus

China's transition to a floating rate regime

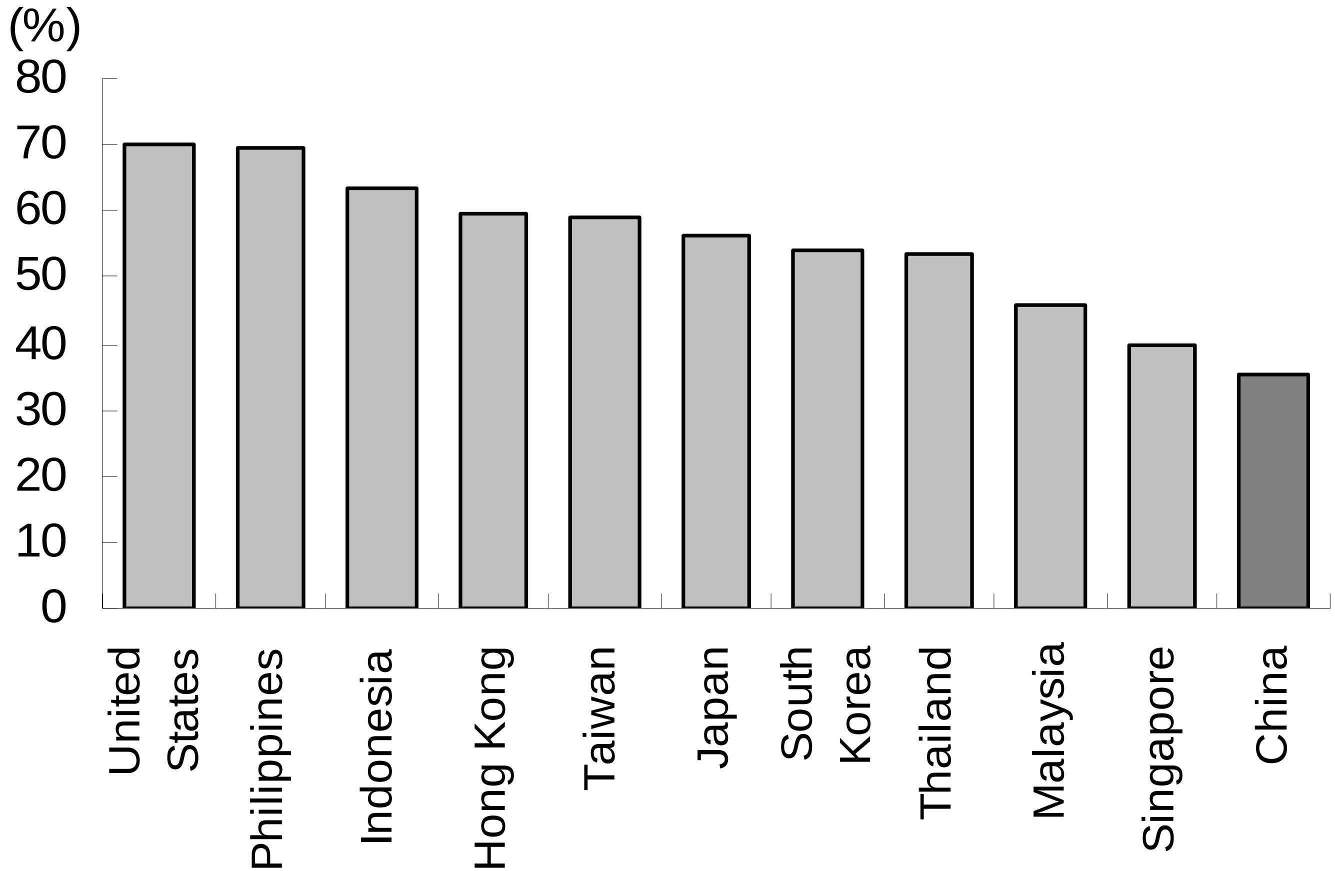
- The need to restore autonomy in monetary policy
- Similarity between China now and Japan in the early 1970s

Changes in current account balances in China and the United States reflecting the savings-investment balance



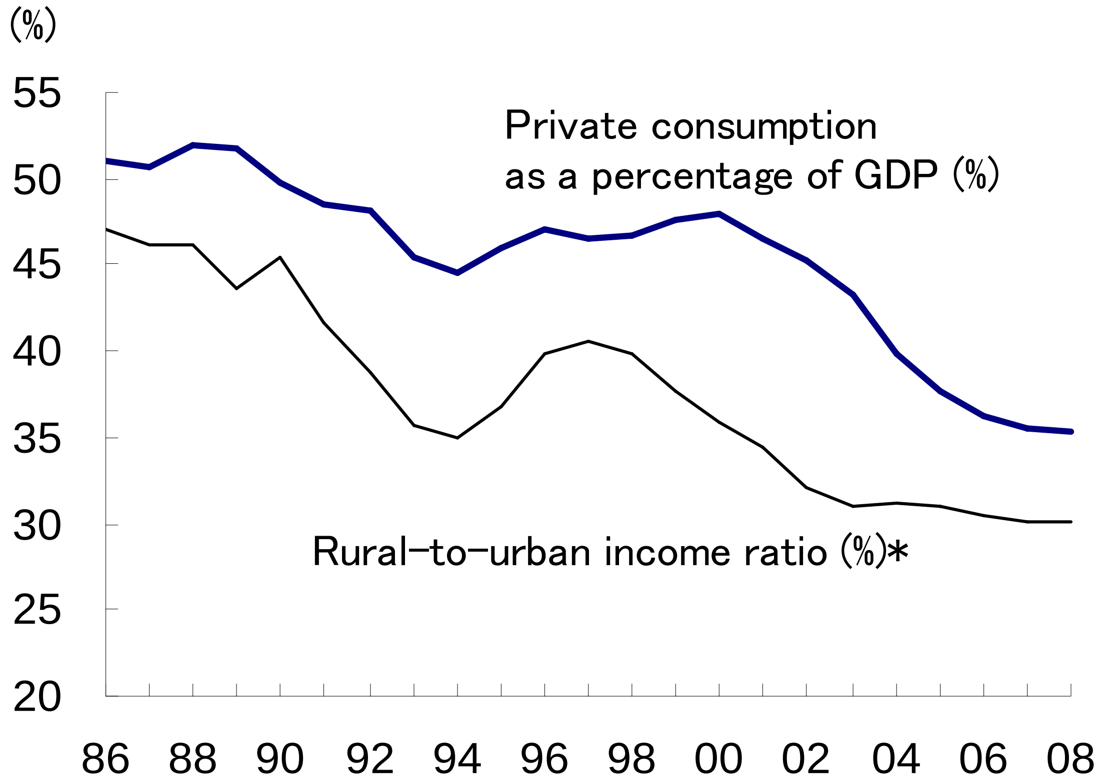
Note: Current account balance ≒ savings – investment
Source: China's statistics based on China Statistics Summary 2009; Statistics for the U.S. and Japan based on the International Monetary Fund's *World Economic Outlook Database*, April 2009

International comparison of private consumption in relation to GDP (2007 figures)



Source: Official statistics for China, Japan, and the U.S.; Asian Development Bank (ADB) *Key Indicators for Asia and the Pacific*, 2008 for other countries and regions

Dwindling private consumption amid widening income disparities

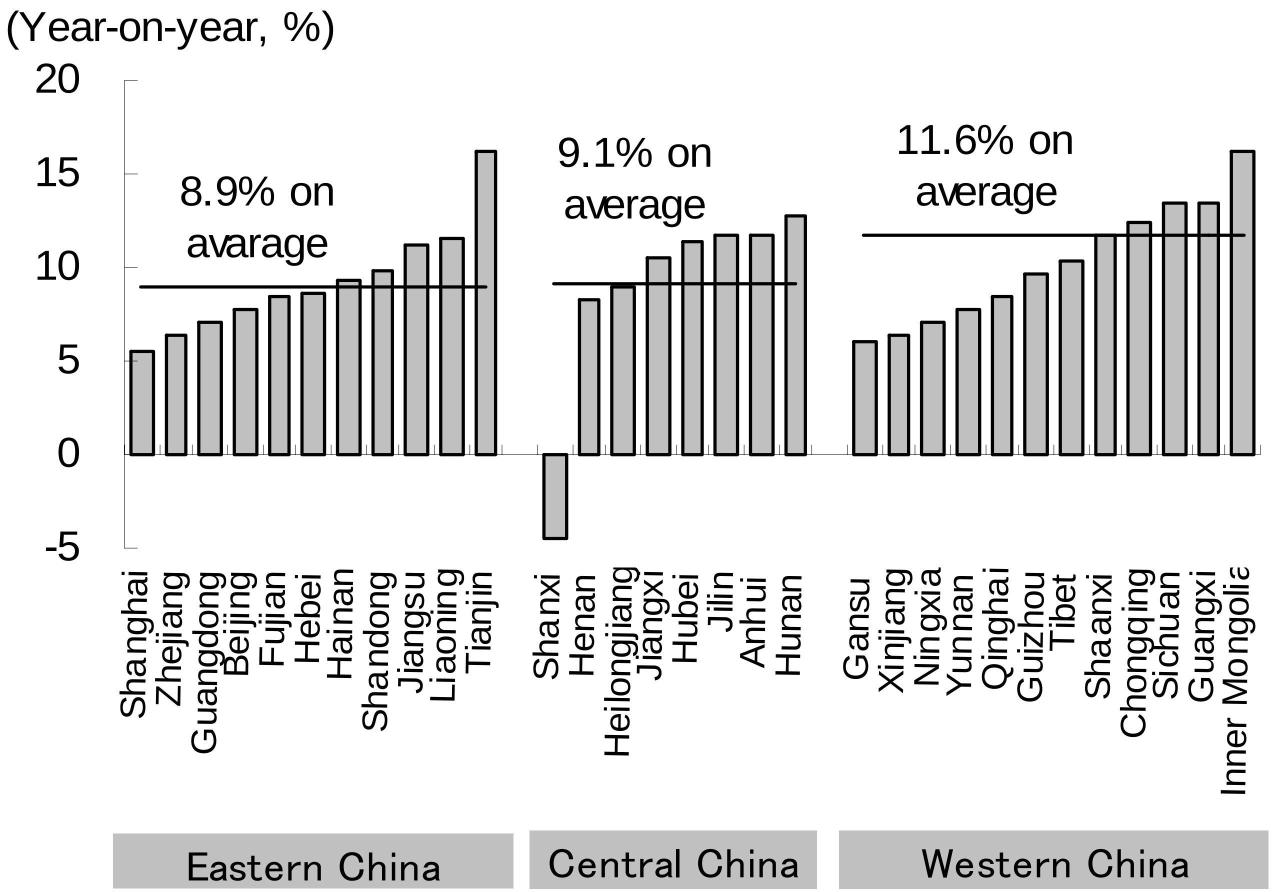


* Per capita disposable income and per capita net income are used to measure urban and rural income, respectively.
Source: *China Statistical Abstract* 2009

Redressing China's regional disparities

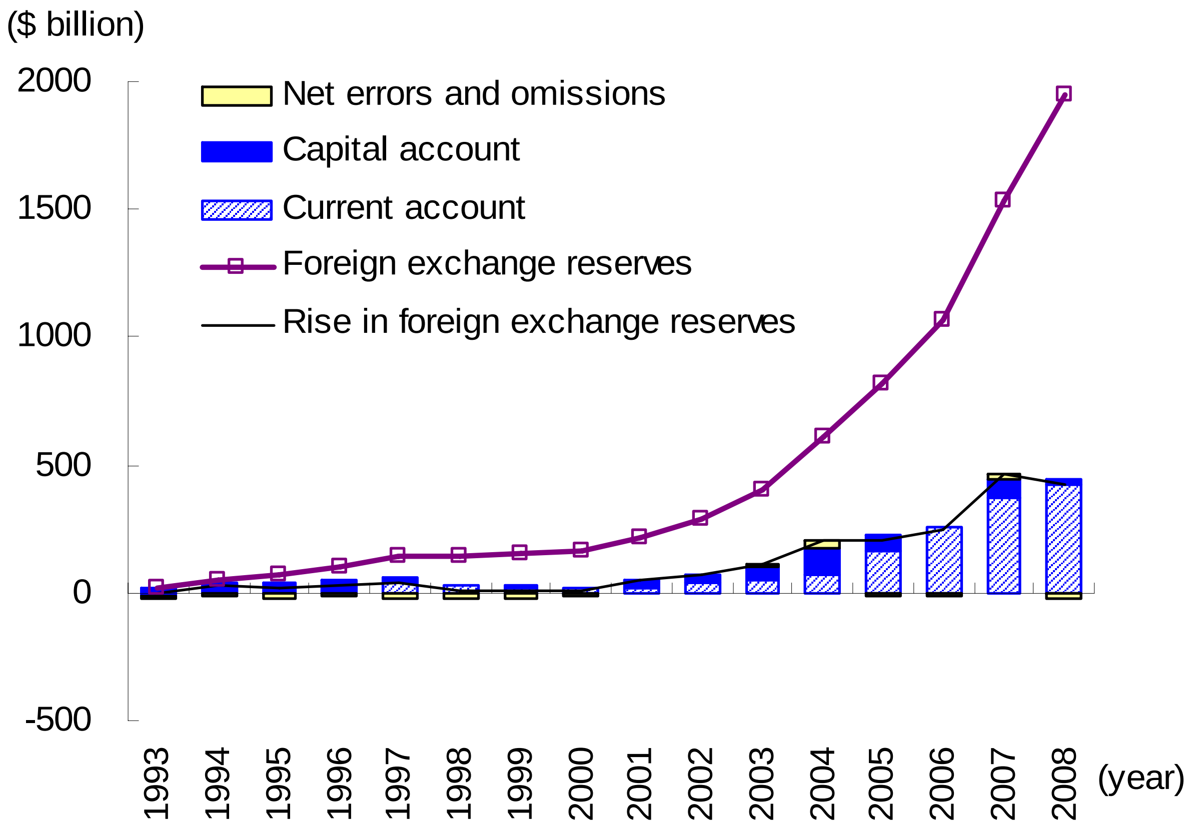
- Domestic FTA
  - Dismantling barriers impeding the mobility of labor (e.g. household registration system), goods, and capital to form a unified domestic market
- Domestic Flying Geese
  - Investment flow from high-income to low-income regions
- Domestic ODA
  - Japan's local allocation tax as a model

Higher growth rates in Western China (first half of 2009)



(Source) National Bureau of Statistics of China.

China's rising "twin surpluses" and foreign exchange reserves



Note: Increase in foreign exchange reserves = current account balance + capital account balance + errors and omissions.
Source: State Administration of Foreign Exchange http://www.safe.gov.cn/

Need to move to a more flexible exchange rate system

- Twin surpluses as the direct result of the government's efforts to maintain an undervalued RMB
- China moved to a managed floating system in July 2005, but has returned to the dollar peg system as an emergency measure
- Moving to a floating rate system needed to restore monetary independence (given rising capital mobility)
- Keeping exchange rate fixed to the dollar will give rise to asset bubble and inflation

The “impossible trinity" in international finance

	Free Capital Mobility	Independent Monetary Policy	Fixed Exchange Rate	Examples
Capital Controls	No	Yes	Yes	China (before July 2005)
Monetary Union	Yes	No	Yes	Hong Kong, EU
Free Floating	Yes	Yes	No	Japan, Australia

Source: Created by author