No Value in Picking a Currency Fight with China

By David Parsley and Helen Popper January 26, 2009

Treasury secretary nominee Timothy Geithner's strong language about China's currency policy was a mistake. Particularly unfortunate was Geithner's use of the term 'manipulator.' If the manipulator designation were made official, it would require the Treasury Department to open formal negotiations with China over its currency policy. Such an approach would be provocative and untimely, standing in the way of what's needed now: cooperation on global fiscal stimulus. The Obama administration should focus on cooperation in support of China's own planned stimulus package, not on futile finger-pointing.

Geithner's comments suggest that China's currency plays an important role in U.S. economic weakness via our trade deficit. His comments reflect the notion that a stronger Chinese currency would make Chinese goods expensive enough to keep us from buying them. This argument is a red herring. China's weak currency – manipulated or not – is not central to our economic crisis or even to our overall trade deficit. As everyone knows, the trade deficit is the gap between what we import and what we export. What not everyone realizes is that the trade deficit is also the gap between what we produce and what we spend. Whatever happens on the yuan front, it is impossible to close the trade gap without closing the spending gap. Any reductions in imports from China would simply be replaced by imports from other countries. So, right or wrong, dogging the Chinese about currency manipulation won't get us anywhere at this point.

What will get us somewhere is coordinating international efforts to stimulate the world economy. Each country, on its own, can stimulate its economy; but each country's stimulus will "leak" a little, invigorating the economies around it too, not just its own. Just as other countries will benefit from a U.S. stimulus, we will benefit from those of other countries.

China has proposed a stimulus package that is roughly twice the size relative to its economy of the proposed U.S. package. We should be encouraging China and all of the world's economic powerhouses – Japan, the United Kingdom, Germany, and France – to move toward aggressive and coordinated efforts on the fiscal front. While these countries all have stimulus packages in the works (some more substantial than others), timely follow-through will be critical. If these packages get delayed, watered-down, or even fail to get enacted, then prospects for a global recovery will be diminished. The Obama administration should be working with these countries, not against them. Moreover, they and the United States collectively should be encouraging additional countries to follow suit. Global coordinated economic stimulus is critical to reviving the world's economy.

The alternative to international cooperation is grim. Geithner's comments raise the specter of a reenactment of the profound international economic policy mistakes of the Great Depression. At that time, each country on its own pursued a policy of currency devaluation in a misguided attempt to spur its own economy at the expense of others. Such bad policies went hand in hand with protectionism; and global trade and economic activity plummeted. U.S. trade alone fell from about $10 billion in 1929 to a mere $3 billion in 1933. In the current crisis, we have already seen a stark downturn in U.S. trade. The latest U.S. figures show that in a single month our exports declined by nearly six percent and our imports declined by twice that. Likewise, both exports and imports have fallen sharply in China.

The current crisis is a global crisis. So, was the Great Depression. A key lesson from those dark times is that the road to renewed growth requires strategies that embrace global cooperation, not mutual antagonism. Let's hope Geithner's statement was merely an unfortunate rhetorical misstep, not an omen of the new administration's future policy.

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