Comments on “Who cares about the Chinese yuan?”

Vimal Balasubramaniam, Ila Patnaik and Ajay Shah

Joshua Aizenman
UCSC and the NBER
March 16, 2011
NIPFP-DEA Delhi meeting
The paper asks key policy questions, applying a useful methodology

- The results, while intriguing, are backward looking.
- I have doubts about the degree to which the results are informative about the future.
- With respect to China, *past performance is not necessarily indicative of future results*...
Methodology

- For a benchmark currency, say CHF, estimate

\[
d \log \left( \frac{\text{CNY}}{\text{CHF}} \right) = \gamma_1 d \log \left( \frac{\text{USD}}{\text{CHF}} \right) + \epsilon
\]

- Apply the residual \( \epsilon \) as in the regression

\[
d \log \left( \frac{\text{MYR}}{\text{CHF}} \right) = \beta_1 + \beta_2 d \log \left( \frac{\text{USD}}{\text{CHF}} \right) + \beta_3 d \log \left( \frac{\text{GBP}}{\text{CHF}} \right) + \beta_4 d \log \left( \frac{\text{JPY}}{\text{CHF}} \right) \\
+ \beta_5 d \log \left( \frac{\text{DEM}}{\text{CHF}} \right) + \beta_6 d \log \left( \frac{\text{CNY}}{\text{CHF}} \right) + \epsilon
\]
Main results

- The GDP-weighted coefficient of the orthogonalised CNY in Asia is small.
- The GDP-weighted coefficient is roughly zero when computed at the level of LDCs and EMs and when computed for the entire world.
- The impact of RMB appreciation upon global aggregate demand will be small, since this will only act through the Chinese current account surplus. It is likely to have a limited impact upon the exchange rate policy choices of other countries.
- As of today, little evidence of RMB internationalization in affecting the role of the RMB in the exchange rate regime of other countries.
Comments

- The paper asks important questions, applying a useful methodology.
- The results, while interesting, provide little information about the ultimate effect of large independent CYN appreciations on global patterns.
- Past performance is not indicative of the future....
Chances are that the past small controlled appreciations of the CYN were viewed as minor events.

- The adjustment to CYN future appreciations would be non linear: close to zero for small changes, large for changes above a threshold, if the changes reflect a regime change.

- See the literature on the fix sunk costs of entry to a market [Dixit, Krugman, Melitz, etc…].
Little unanticipated variation in the CNY implies limited information associated with regression analysis

- The results probably reflect the fact that, during most of this period, the CNY was de facto pegged to the dollar.
- The absence of sizable unanticipated variations in the data limits the power of econometric inference, even if the authors use the best econometric techniques.
A political economy view of the CYN history

- The changes of the CYN so far were the outcome of pressure of the US congress, under the gun of a tariff threat. There has been no regime change, and the market has good reasons to view the appreciations, so far, as minor innovations without signalizing a regime change.
If one should speculate about the future development of the CYN…

- Chances are that the process of the internalization of the CNY has been and would be controlled tightly by China.
- When China will decide that the time is right, they will do it in a big way.
- When this will happen, it will signal a regime change, and the impact of it would be large.
- The Euro gained 10% of the global market share of IR in it’s first ten years…
Chinese development process, so far, is much faster than that of Japan, Korea etc… at comparable stages.
Thanks for your attention

http://crisiscartoon.blogspot.com/