Chinese labor gets even cheaper with devaluation of renminbi yuan

by Cho Wen-pin

For the past three months, the official swap rate of the Chinese renminbi yuan (the yuan being the unit of account of the RMB or "people's currency") has dropped by about 20% to a historic low against the skyrocketing value of the U.S. dollar on the local exchange centers where currency trade between regions and companies is arranged. In the last few weeks, the U.S. dollar rose more than 10%, reaching 8.5 yuan on official exchange markets at the end of February, while the official rate remained at 5.75 yuan to the dollar. Black market rates have soared even higher, hitting a high of more than 10 to the dollar. Speculators from the financial sector predict that the official rate will rise from the present 5.75 yuan down to as low as 10 to the dollar (see **Figure 1**).

This situation has alarmed some economic experts, yet nothing has been done to curb the decline of the renminbi yuan, which raises the costs of imported machinery and technology desperately needed to industrialize the backward country. A cheaper Chinese currency encourages cheap labor and labor-intensive and export-driven industries within the coastal Special Economic Zones, increases costs of both China's industrial and agricultural production across the nation, reduces economic returns, and discourages investment in infrastructure to develop the interior. It also encourages Chinese workers to convert their savings from renminbi account into foreign currency accounts, or into gold and other valuable articles.

Beijing drives down the currency

Recently, western papers have been full of reports on the Chinese economic miracle, but the currency devaluation indicates just the opposite. As one Japanese diplomat put it: "We think it very strange that the Chinese currency should be depreciating. It should be stronger."

These circumstances are very much associated with government efforts to sell Chinese labor cheap and build up its foreign reserves to save the communist power by adopting the free market economy and becoming a member of the General Agreement on Tariffs and Trade (GATT).

Officials at London's Royal Institute of International Affairs (RIIA) explain that Beijing is being forced to crawl to GATT by the Clinton administration's threat of trade sanctions. At the same time, the United States is also using the threat of trade sanctions, such as the 301 trade clause, to push Taiwan into GATT. But the striking truth is that a united front of western financial interest groups and bankers, not only the United States, have pushed efforts to link Most Favored Nation (MFN) trade status with improvements in human rights and other issues in order to push China into GATT, and consequently to totally open up the country to the world "free market."

"In our progress to build a market economy, we will not resort to administrative measures to set an exchange rate on the open market, which can only mean a regression from ongoing economic reform," said Yang Gonglin, a spokesman for the State Administration of Exchange Control, in early February. While Yang told the truth on Chinese progress toward a market economy, he lied in denying that China will not resort to administrative measures to regulate the exchange rate.

Beijing is deliberately pushing its currency lower to boost cheap-labor exports.

"China must try to get into GATT, because if they could, it would be impossible for the U.S. then to use political arguments to remove China's Most Favored Nation trade status," said RIIA Asia-Pacific Director Peter Ferdinand. But GATT demands that the renminbi be convertible into U.S. dollars.

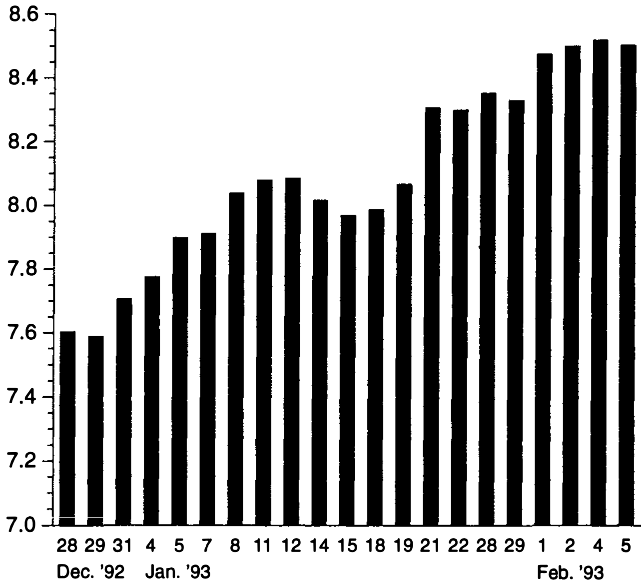
Renminbi devaluation spells turmoil

An imminent steep devaluation of the renminbi is in preparation for full convertibility to bolster China's application to rejoin GATT, which will cost 20 million jobs over and above the huge unemployment rate today resulting from the bankrupting of major backbone industries in China. Although it is not Washington's policy to urge China to devalue the renminbi yuan because of the rising U.S. trade deficit with China, it is nevertheless being urged by western bankers who are part of the century-old colonial condominium. The name of the game is "chop therapy" for both countries.

First, it is the Chinese government's intention to lower the renminbi as its only effective means to control foreign consumer goods from flooding into China, to protect the so-called "national industry," if there is any, since GATT will cut up to half of the average tariffs that have been imposed up till now.

The outcome of this foolish policy will be that China's economy will head toward export of cheap goods, and the "national industry" will be turned into sweatshops, supplying goods to stores such as K-Mart in the United States. Meanwhile, it devalues domestic wages and the return on investment in the industries with foreign investments targeted for export. Those joint ventures, which need to import raw or semi-raw materials, will face a high risk of bankruptcy.

FIGURE 1
Dollar rises against yuan
(Yuan per U.S. $)



Source: *EIR.*

Furthermore, it drives these industries to look outward for consumers and to sell cheap since the rest of the world economy is undergoing a depression, too.

Second, while the renminbi continues to lose value, foreign investors are holding on to their hard currencies, which are needed to upgrade old technologies in the manufacturing sector by importing newer and better hardware from the industrialized countries. Without advanced technology and new forms of energy, like nuclear power, for instance, there is no chance for industry to catch up to foreign competitors in 3-5 years. The idea behind the U.S. policy to push China into GATT reflects demands from western bankers to allow organized capital flight.

Third, like these companies, Chinese consumers are also inclined to change their savings into foreign currencies or to buy gold and other valuable items which keep their value. In Shanghai in mid-February, Chinese private investors rushed to open foreign currency accounts.

"Citizens are opening more than 500 foreign currency deposit accounts with the Bank of China's Shanghai branch every day . . . but before they were opening only 150 new accounts a day," reported China News Service. "The recent craze of foreign currency savings was mainly triggered by the gradual downturn adjustment of renminbi, thus making the U.S. dollar a hot currency to keep," as rumors that a sharp official devaluation is imminent encouraged Chinese to dump yuan banknotes on the black market for U.S. and Hong Kong dollars.

In Beijing, residents have been snapping up gold as a hedge, and the price of gold jumped 20% from the beginning of the year to mid-February, and sales were double during that period compared to last year, as reported by the *China Youth Daily*. In Guangzhou and other coastal cities, the Hong Kong dollar has gradually ousted the renminbi yuan as the booming region's preferred medium of exchange, which is accepted virtually everywhere.

Fourth, any Chinese investors from the mainland and overseas as well as western entrepreneurs who are attempting to produce tangible goods for both domestic and foreign markets, obviously now prefer getting loans from the government and private banks in China rather than using their own capital and risking a fall in future value, which aggravates inflation. Due to the fact that the government is also decentralizing the national banking system, loans from the privatized banks are to be issued under higher interest rates in order to collect money by installments, reviving old practices of usury.

Since the end of last year, foreign investors have had a hard time obtaining foreign currency from the Chinese Central Bank. Without dollars, China's influx of foreign investors is finding it difficult to import machinery and raw materials.

Finally, the fact is that the surging dollar is a symptom of an overheated economy and one danger sign pointing to higher inflation, as renminbi devaluation proceeds. The problem is that when inflation rises, the government has to encourage private investment, i.e., to issue government bonds and to sell bankrupt state-run industries. China is furthermore privatized; the central government concedes power to the regional or provincial governments, losing its capability to collect taxes from individuals and local authorities when the country requires money, not only to cut its huge deficit, but to invest in infrastructure, medical care for the elderly, and education for the young, especially in a period when the immature and backward national industry has yet to be jump-started.

So far, the response from the Chinese government seems to be to let "free market forces" set the level of its renminbi currency unit, based on the idea that Adam Smith's "invisible hand" will set prices of consumer goods and appraise bankrupted manufacturers. Consequently, some of the potential manufacturers could be underestimated, and labor costs therefore are undersold.

While the country stresses tertiary industries and market speculation—a "third wave," as termed by Alvin Toffler—new established enterprises do not have an incentive to buy obsolete "second wave" and energy-consuming equipment, which were built in the past 40 years.

Chinese 'maquiladoras' won't help

This idea of *maquiladora*-style sweatshops along the Chinese coastal areas has been experienced for a decade. Last year, the country had a burgeoning trade surplus, but the question is, where are the dollars it earned? If the 12.8% growth rate for 1992 is true, then why, as reported recently by the Chinese Academy of Social Sciences, is there increasing social unrest?

According to the latest statistics published by the International Labor Organization, China ranked 49th in world textile production in terms of labor cost in 1991, at $0.34 per hour, much lower than developing industrial regions in Asia, such as in the Association of Southeast Asian Nations (ASEAN) countries (except Indonesia). The question is, if these manufacturers laid off some of the employees and paid the wages to the rest, giving them an average salary of $0.42 per hour, an increase of 20% to every worker's income, do we call that an economic miracle?

As reported by Xinhua on Feb. 24, an investigation has shown that China's textile industry will shed 2.5 million jobs out of 7.5 million workers and staff in the industry. According to the study, "China is losing its advantage of cheap labor." It further suggested that old textile factories should be "closed to real estate, commercial, monetary and information business sectors."

But Hungary, former Yugoslavia, Poland, and Russia have demonstrated that China can't survive if the Chinese government simply makes a 180-degree turnaround, heading for the equally disastrous "let the world market decide all" ideology.

The only solution for Chinese economic development is the issuance of Hamiltonian-style credit from the central bank, specifically to encourage new enterprises to produce tangible goods and to expand the work force, which would expand the tax base, and to use both its credit and foreign reserves to upgrade technology, unleashing the productivity of old industries. Concurrently, the government must establish an effective system to collect tax revenue from private individuals and enterprises, reversing the current situation where the government does not collect taxes from owners of privatized companies due to lack of efficient taxation enforcement.

The Chinese economy also requires an extensive investment in infrastructure, and a balanced development of agriculture and industry, or a division of labor designed primarily for the domestic market, which has 1.2 billion people, who need food, clothing, housing, transport, energy, communications, hospitals, and education.

Also, the government must cool speculation against the renminbi yuan, and stop its slide against the dollar on the currency swap markets for businessmen.

Chinese economic experts and other social institutions have to advise the government to adopt economic, legal, and administrative measures to combat the rise of foreign currencies and fall in value of Chinese labor, and to set the rate at the amount of renminbi it takes to earn $1 accounted on both domestic and foreign markets, with the provision that industry and agriculture which produce tangible goods are given first priority.

Freedom to choose the good

Beijing now holds students and workers, who expressed even their limited demand for freedom, as political hostages to bargain with the world. These prisoners are selectively released when Beijing needs to dicker with foreign forces or to repair its own image. For instance, Wang Dan, a student leader of the Tiananmen Square protests who had been number-one on the most-wanted list, was paroled a few weeks ago. His release is widely viewed as a gesture to President Clinton, Governor Patten in Hong Kong, and even President Lee Tenghui in Taiwan as an attempt to demonstrate that China is improving its human rights record. But it happened for two major reasons.

First, there is a yearly renewal of MFN status that has to be passed by the U.S. Congress and signed by the President. The MFN issue has been attached with human rights conditions for the past three years after the Tiananmen Square massacre, although President Bush vetoed it again and again. Clinton vowed during the campaign that he would be tough on China's humanitarian record, and he has gotten a few people released. One interesting point of this MFN controversy, is that when human rights conditions are applied, only Chinese private businesses can enjoy this trade benefit, not the state-run industries. This is obviously leverage to privatize China.

Second, a protection bill initiated by Nancy Pelosi (D-Calif.) and others was passed last year by the Congress, and signed by Bush during the campaign when his China policy was under an attack from Clinton. Regulation from the bill states that if the President can't prove to the Congress that China's human rights record has been improved, some 80,000 Chinese nationals who entered America before April 1990 would possibly be granted permanent residency (green card status) on a case-by-case basis.

Confucian economic principles

A sound economic theory can only be constructed on the basis of a profound philosophical understanding of universal truth. China has 5,000 years of history marked by fights between the Confucian economy on the one hand, and legalism-Taoism's effort to demolish Confucius's principles as they were defended by Mencius in Ancient China, Chu Hsi during the A.D. 1120-1200 period, and also in this century by Dr. Sun Yat-sen.

Beijing has to adopt Sun Yat-sen's three principles of true republican statecraft, which is coherent with physical economy. To build a better economy, China has to give up the illusion of free trade, and to free its political prisoners.

But the Chinese communists, it appears, would rather choose Adam Smith's "free market economy" than employ the principles of Confucian humanism and of Sun Yat-sen.