

Bloomberg Radio / News **The Final Word – May 18, 2007**

Interview: Robert Lawrence Kuhn, Ph.D.



Steve Geimann, Host:

China has acted to tame its runaway economy and ease trade tensions with the United States and Europe. The government in Beijing has raised the amount its currency can appreciate. It has lifted interest rates and curbed bank loans. China announced these actions on the eve of top-level meetings between Treasury Secretary Henry Paulson and Chinese Vice Premier Wu Yi.

Robert Lawrence Kuhn is a Senior Advisor to Citigroup Investment Banking. He just met with senior officials in China. Robert, why did China increase the range for its currency right on the eve of these meetings in Washington?

Dr. Robert Lawrence Kuhn, Senior Advisor to Chinese Government, Citigroup:

Steve, you have to understand that this is a Party Congress year in China. A Party Congress occurs every five years, and it's the most sensitive time for political policies and personnel appointments at the highest levels. Stability of the country is always China's highest requirement and this is absolutely true in the run-up to a Party Congress. That is a primary context factor for evaluating government policies.

Sure, we have the upcoming meeting between Vice Premier Wu Yi and American senior officials; and, sure, China wants to avoid a confrontation with the U.S. Congress over trade and currency, which would impose even greater difficulties on China.

Consider China's rural population – two thirds of the population – whose income is substantially lower than China's urban population, a vast disparity that has become China's most pressing domestic concern. The agricultural productivity of these farmers is not especially efficient, so already they are only marginally competitive, so that if the yuan appreciates, their food products will be even less competitive and the income of rural workers would fall, further exacerbating the income disparity and opening up society for serious social unrest, which is the last thing that China wants. Hence all policies have to be viewed from the perspective of domestic stability, particularly this year.

Geimann:

And are these steps they announced today, in combination with some steps a couple of weeks ago, going to be enough to slow the economy down from an eleven percent growth rate?

Kuhn:

The combination of steps certainly helps, and it's certainly in the right direction. There's another problem, too -- the white hot runaway stock market prices. For years, China's stock market languished and the government tried to propel it. In the last two years, it's more than tripled – even up 50 percent this year – so that officials worry that the bubble may burst, which would make millions of investors very dissatisfied – again a danger in this year of the Party Congress.

So part of the reason that the government has raised bank deposit rates, even higher than they raised the bank lending rates, is to encourage people to put more of their money in banks as opposed to the stock market.

All of these steps must be looked at together, as modest steps forward, designed to solve multiple problems. China works by evolution not revolution – small steps, trying them out, nothing traumatic. And each of these steps need to be considered as mechanisms to avoid social unrest.

Geimann:

What do you expect to occur after the meetings next week between Paulson and the Chinese Vice Premier?

Kuhn:

Generally, in going into these kinds of meetings, both sides are positioning, sometimes reducing expectations; and then afterwards, in almost every case, each side says that they've achieved what they sought, although in reality, it is often not as much as they had wanted to.

With Wu Yi and Henry Paulson, we have two very smart officials and who are very sensitive to all the issues, but both have constituencies that are problems for them. Obviously, the Democratic-controlled Congress is making an issue of American loss of manufacturing jobs. Wu Yi has a similar problem in China [where officials fear that significant appreciation of the Yuan will throw millions of workers out of work]. Both will work together to try to satisfy both sides.

Geimann:

Robert Lawrence Kuhn is a Senior Advisor to Citigroup Investment Banking. He just met with senior officials in China to discuss next week's meeting and today's actions by the Chinese to help cool down their economy.