opinion

To avoid the currency wars

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Washington

The global economy needs exchange rate coordination now. Absent that, the world is likely to be increasingly afflicted by exchange rate fluctuations and policy acrimony. These are bound to undermine the economic recovery and increase the likelihood of stagnation.

In 2010, Brazilian Finance Minister Guido Mantega warned of the possibility of "currency wars" as countries sought to devalue their exchange rates to gain competitive advantage.

Brazil's economy may currently be less in favor internationally, but that doesn't change the validity of Mantega's concerns. In a world of demand shortage, a weaker currency can increase demand for a country's goods — and thereby help with its own economic recovery.

The undeniable problem is exchange rate devaluation benefits the devaluing country at the expense of others. From a global standpoint, it can easily become a case of robbing Peter to pay Paul.

The Great Depression of the 1930s provides warnings along such lines. Back then, the depression prompted competitive depreciation and trade conflict as countries sought to gain demand by increasing exports and lowering imports. That process contributed to deepening the depression.

Today the problem of exchange rate conflict is again on the rise. One problem is China's long-running trade surplus with the United States. Those surpluses should long ago have fostered steep renminbi/dollar appreciation to rebalance the trade account.

Yes, the renminbi has appreciated somewhat in recent years. But it is has not been enough to prevent the U.S. trade deficit with China from steadily increasing.

Instead, China has intervened in markets to limit the scale of exchange rate appreciation. The country's goal remains to retain both export competitiveness and attractiveness as a destination for foreign direct investment.

A newer and much more difficult problem concerns quantitative easing (QE). Under this process, central banks buy domestic assets on a massive scale to lower interest rates. Indeed, Mantega's comments were actually spurred by the U.S. Federal Reserve's QE program.

The core problem is monetary policy interventions inevitably have exchange rate impacts in a modern economy with flexible exchange rates and internationally open financial markets.

When a central bank increases the money supply by buying domestic assets and lowering domestic interest rates, some of that money is diverted offshore as investors seek other investment opportunities. That move offshore causes the exchange rate to depreciate.

The justification for QE in the United States was strong. The country's economy was in deep recession, long-term interest rates were still quite high and the U.S. government was running large budget deficits. It clearly needed assistance with financing to keep interest rate costs down.

But at this juncture, things are getting complicated. In Japan, the new policy of "Abenomics" involves massive central bank purchases of Japanese government debt. Japan's 10-year interest rate is already at 0.88 percent. The principal impact of Abenomics is turning out to be yen depreciation.

By buying bonds and flooding the market with cash, Japanese investors are being given the incentive to go overseas in search of yield. And to buy foreign assets, they must sell yen. That has not only already triggered a wave of yen-dollar depreciation. It also promises to trigger other exchange rate changes that increasingly resemble global competitive devaluation.

The problem is that, on the surface, Abenomics looks a lot like QE. Consequently, how can the United States or other nations object?

From an international perspective, the problem is not QE — but the pursuit of QE within a flawed framework. The solution is exchange rate coordination.

Given the global economy's demand shortage, the world needs easy monetary policy that lowers interest rates and facilitates budget deficits. However, such monetary policy must not be allowed to impact exchange rates. International coordination of exchange rates by central banks can accomplish that.

Such a system needs rules of exchange rate intervention. Historically, the onus of defense has fallen on countries' whose exchange rate is weakening, which requires them to sell foreign exchange reserves. That is a fundamentally flawed system because countries have limited reserves. Speculators therefore have an incentive to try and "break the bank" by shorting the weak currency. They have a good shot at success, given the vast scale of low-cost leverage financial markets can muster.

George Soros proved that when he successfully bet against sterling and the Bank of England in 1992.

A new, smarter international system must share the onus of intervention with the country whose currency is appreciating. Its central bank has unlimited amounts of its own currency for sale, so it can never be beaten by the market.

Consequently, speculators will back off if this intervention rule is credibly adopted, making the target exchange rate viable.

Intervening in this way will also give an expansionary tilt to the global economy. When weak currency countries defend their exchange rate, they often raise interest rates to make their currency attractive, thereby imparting a deflationary global bias.

If strong surplus countries do the intervening, they may lower their interest rates and impart an expansionary bias. The bottom line is a sensible coordinated exchange rate system can both stimulate the global economy and help avoid looming international economic policy conflict.

The means for such a system are at hand, but so far the politics have lagged. In the United States, discussion of exchange rate policy has been blocked by two factors. The first is simplistic free market nostrums and the second a legacy of misunderstanding from Chicago School monetarism that claims exchange rates do not matter because induced depreciation will be offset by inflation.

The only silver lining to the Great Recession is it has dented Chicago School economics. That has created new policy space, but so far political leaders have failed to take advantage. That must change.

The September 2013 Group of 20 summit in St. Petersburg provides an ideal opportunity to launch an initiative for exchange rate coordination. Not only would it address the problem of currency war, it would also build market confidence by showing that the world's political leaders can still work together on matters of vital economic import. Carpe diem.

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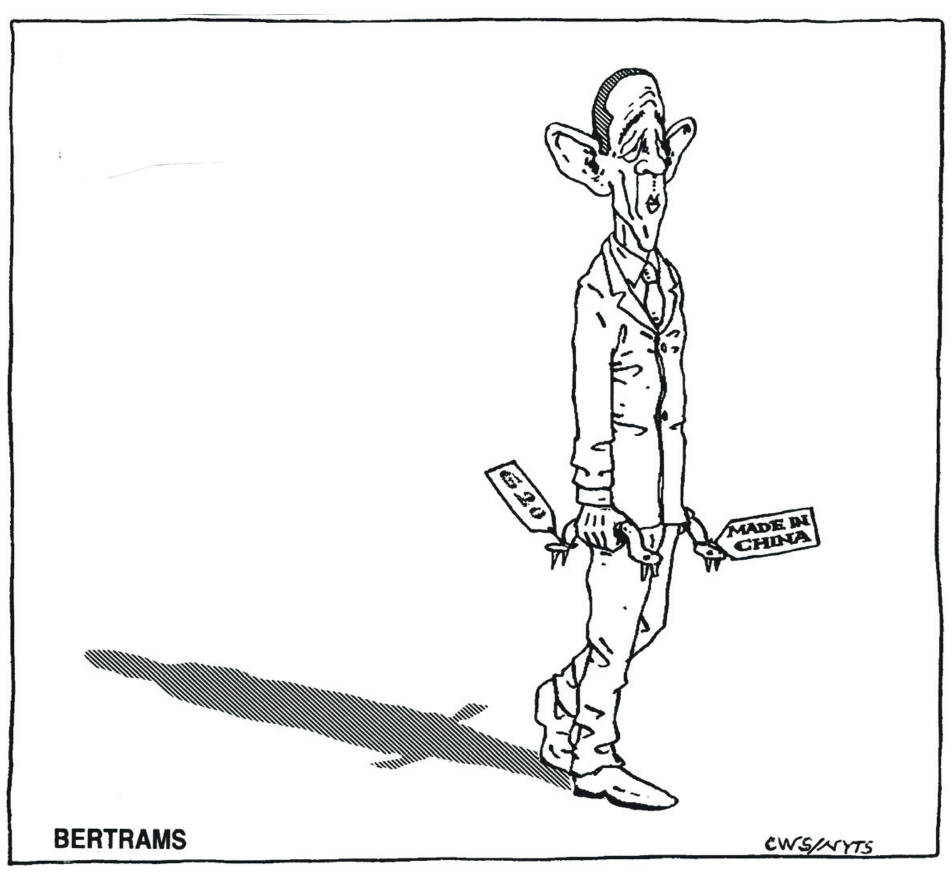

Too early to talk about 'Likonomics' in China

William Pesek
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Let's have a moratorium on the word "Likonomics"? Premier Li Keqiang's plans to overhaul the Chinese economy have hardly earned such a grand moniker yet.

Say what you will about "Thatchernomics" or "Reaganomics," but Margaret Thatcher and Ronald Reagan fundamentally altered the British and American economies. No one is rolling their eyes at "Aquinomics," President Benigno Aquino's thus-far successful prescription for the Philippines, the onetime "sick man of Asia." By contrast, Likonomics is a ridiculously premature nod to ideas that are, at best, still on the drawing board and might never come off it.

In Japan, economists and a cheerleading media now seem to realize they bought into "Abenomics" too hastily, creating the myth that Prime Minister Shinzo Abe's revival plan is succeeding when it has only just begun. Game-changing reform efforts take several years to implement. We are a long way from knowing if Li has the skill or political will to manhandle China onto a more sustainable growth path, led by domestic demand.

How will we know? There are three clues to whether Likonomics is more than a hollow slogan.

First, can Li avoid further stimulus?

The premier's supposed shock-therapy program already has its own myth: that China is engineering a sharp slowdown. Li doesn't WANT growth to slide toward 5 percent — no Chinese leader in his right mind would at a time when protests are becoming commonplace. Rather, China's export- and investment-led growth model is burning out on Li's watch.

Well before Li and President Xi Jinping officially took the reins in March, exports were falling, manufacturing was contracting and economists were downgrading forecasts. Big reforms are always easier when growth is booming. If Li could wave a magic wand and get gross domestic product back into double-digit territory without pumping more air into China's credit bubble, he would in a Shanghai minute. He needs reasonable growth to stabilize his power base and figure out how to turn the economy upside down without crashing it.

At the same time, Li's program is about "deceleration, deleveraging and improving growth quality," according to economist Huang Yiping of Barclays Capital Asia Ltd. in Hong Kong, who is credited with coining the term Likonomics. Carrying it out will hasten China's downshift. The premier is sure to face mounting calls for the government to throw new cash at the economy — from businesses and from 1.3 billion Chinese, who are becoming more vocal and defiant.

Li himself has pledged that China's growth and employment will stay above a certain floor. That raises doubts about whether he's ready to accept the pain necessary to see through his reforms. Economists are already buzzing about a "Li Keqiang put" not unlike former Federal Reserve Chairman Alan Greenspan's. More stimulus would only exacerbate China's overcapacity problem and make the eventual debt reckoning bigger and costlier.

Second, is Li ready to allow a headline-grabbing default or two?

The secret to China Inc.'s success has been plentiful and mispriced credit. Reckless borrowing, largely through local government-financing vehicles, was the fuel behind China's years of double-digit growth. Special-purpose companies set up by authorities across China used this cheap money to fund giant infrastructure projects.

Companies such as China Rongsheng Heavy Industries Group Holdings Ltd., China's biggest shipyard outside state control, are already begging for bailouts. Entire cities such as Ordos — a white-elephant project in Inner Mongolia — need help, too.

According to the National Audit Office, the brand of financing vehicles that got Ordos in trouble amassed totaling $1.7 trillion at the end of 2010 (you can bet it's much, much higher now).

Only after a big default or two will markets begin to price Chinese risk appropriately, allowing Beijing to liberalize interest rates. Is Li willing to accept the consequences — turmoil in markets, mass unemployment and credit downgrades?

That's nothing compared to the third test: inviting the Communist Party's wrath.

There's ample reason to doubt Li's doctorate in economics will help him navigate Beijing's cutthroat politics. If you think Abe faces resistance from vested interests, imagine what awaits Li as he tries to get Communist Party power brokers, ambitious regional leaders, a vast network of state-owned companies and the Chinese people to make sacrifices.

Li must take on thousands of party stalwarts who make millions, or billions, of dollars from dodgy land grabs, insider trading and old-fashioned rent-seeking. Politics will stymie Li's every effort to reduce the state's role in the economy and create the vibrant private sector China needs in order to thrive. We'll have a sense of whether he's serious when the number of unnamed-source gripes in the official media starts to spike.

We are years from knowing if Li can live up to the example set by Deng Xiaoping, who truly did revolutionize China's economic system.

If Li can, Likonomics will deserve to go down in history as a model for developing nations everywhere. Until then, let's give the phrase a rest.

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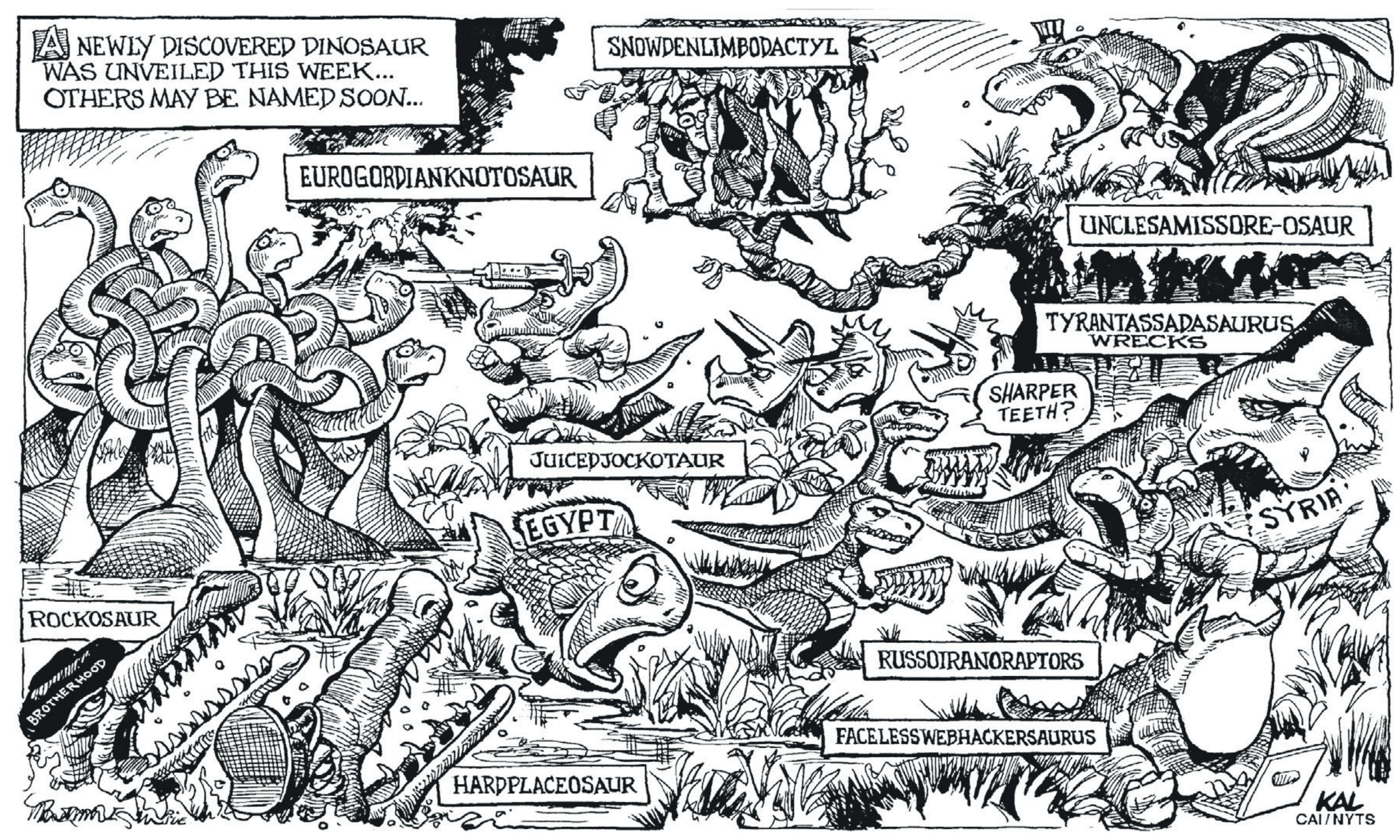

Letting the changes out at the beach

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I've just returned from two weeks on a beach in southern Europe, where a curious gender divide manifested itself. While the women of the party fought off an attack of melancholy because they were missing out on a domestic heatwave, any men in the vicinity scratched their heads.

"Why would you care what's happening somewhere else?" they asked. "We're here." Why FOMOOH (Fear of Missing Out on Heat) isn't an equal opportunity regret is indeed a mystery, but in the event it mattered not. A far greater liberation awaited us.

Even the most high-minded of readers will be aware of the seasonal phenomenon that triggers a creeping paranoia in many women and some men, resist it though they know they should. It involves some combination of the words "beach," "body," "bikini" and "ready," and is often accompanied by photographs, either of a preternaturally perfect quasi-human frolicking through the surf or, conversely, of someone all too obviously human, with their lumps, bumps and sundry other physical imperfections circled in red lest we should be in danger of failing to notice them. Impossible eating regimes may feature and, perhaps worst of all, pre-holiday "cheats."

Avoid the former and never be tempted to try the latter; an artfully ruched T-shirt or cinched-in wide belt will never make you look two stone lighter. It may simply make you look like you are unable to dress yourself with even a modicum of taste.

You may think these flesh-hating features and sidebars of shame have nothing to do with you, but they are so culturally pervasive that I doubt anyone is entirely beyond their reach.

Wait a minute. I'm wrong. This might all be going on in the pages of magazines and the tortured synapses of holiday-makers, but it sure isn't making it to the beach.

On the shores of northwestern Crete, an island admittedly unacquainted with the small portion, bodies refused to be confined, either by contemporary mores or, in fact, by their actual swimwear.

Every way you looked, breasts heaved and bottoms spread and — predictable joke ahoy — that was just the chaps. (Incidentally, if we were to elect a figurehead for the campaign for real body shapes on beaches, it would have to be the bronzed and mustachioed bloke in Speedos from the advert for Southern Comfort currently gracing our TV sets.

I suspect that, while the semiotics of the ad suggest that we should scorn this brave fellow, we are all secretly attracted to him. Why? Do I really need to explain?)

In my Greek idyll, the tiniest of bikinis and the most imagination-sparing of budgie-smugglers battled heroically to preserve their wearers' modesty and, more often than not, lost the fight; there appeared to be little call for that most buzz-killing of garments, the beach "cover-up," unless it was to form a tablecloth for an impromptu seashore picnic (more bulging tummies). My beach buddies were, physically and metaphorically, letting it all hang out.

One afternoon, I watched two friends stroll in relaxed fashion along the water's edge, both of them young women of unknown nationality. One was slender and the other a great deal larger. They were matching bikinis. To the casual glance, it didn't appear that they were discussing how to expunge carbs from their diet or the pick of the latest anti-cellulite creams; they looked too happy for that.

Why do we do this to ourselves? Answer: we don't. We allow others to do it to us and we should stop. Here's how: It's not simply about using all beach-related propaganda to line the cat-litter tray, although that's a start; more crucially, it's about refusing to believe in the mythical beach for which you are meant to be preparing yourself. It doesn't exist.

Outside of some highly exclusive resorts, which may well have a pair of scales tucked beneath each lounger and a cosmetic surgeon on call, the beach-ready body is a chimera, destined only to trap us in a world of self-hatred and body fascism (and to sell magazines). But luckily there is another way: in the free world, you are more likely to find sweaty, wobbling bodies blissed out on ice cream and sexual abandon than uptight fitness freaks with washboard stomachs and six-packs.

Perhaps the physical laissez-faire that I witnessed occurs particularly when people have real things to worry about.

In Crete, we discovered that it was almost impossible to pay for goods and services with anything other than hard cash; a credit card was greeted with blank and unwelcoming stares.

In a butcher's shop, I found myself looking for the odd change to settle the bill with the right money; the man behind the counter waved my coins away.

"Thirty cents won't save me," he laughed. "You or the shop?" I asked. "Me, the shop, Greece," came the reply.

The one thing that remains in plentiful supply is food itself and the Cretans, famed for their hospitality, seem unwilling to allow hard times to curb the pleasure they take in satisfying their appetites. Lest this all seem like an excuse to fall greedily on another plate of calamari or a third flagon of retsina, while doing little more to burn off the calories than reclining on an air mattress or leafing through a paperback, here is another thing to consider.

Also among my holiday companions was a small girl, enjoying perhaps the first experience of abroad that she will actually remember and particularly keen to launch herself into the waves at every opportunity. Her unfettered and unself-conscious enjoyment in her own physicality, in the rays of the sun and the warmth of the sea, was a delight to behold.

The thought that she might one day cringe at the sight of her own body, to measure it against an oppressive and entirely arbitrary standard and find it wanting, makes me want to rip up every image of so-called poolside perfection into a million tiny shreds.

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Southern Thai separatists reach trust milestone

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Peace talks between the Thai government and Muslim separatist groups reached a milestone last month when the two parties decided to sit down to discuss ways to rebuild mutual trust and eliminate suspicion and to find a long-lasting solution to the protracted conflict.

Malaysia, once accused of meddling in the unrest in Thailand's deep South, hosted the peace talks in Kuala Lumpur on June 13, between representatives of the Thai government and members of the Barisan Revolusi Nasional (BRN).

At the end of the meeting, a statement was released vaguely stipulating the importance of good will and sincerity, but without specific measures on how to reduce violence. The issuing of the statement was timely, just ahead of the Islamic holy month of Ramadan that began in July.

Despite optimism, the challenges have remained. Although the two parties have already had three rounds of talks, killings in the restive South — particularly in the provinces of Pattani, Narathiwat and Yala — have continued. The Muslim militants have mainly targeted security forces and teachers, perceived as agents of the predominantly Buddhist Thai government.

Under the government of Thaksin Shinawatra (2001-2006), an Islamic insurgency re-erupted in 2004. The incidents at Krue Sae Mosque in Pattani, where 32 Muslim militants were executed, and at Tak Bai district in Narathiwat, where 78 Muslim detainees suffocated to death while being transferred to a long-distance military camp (they were tied behind their backs and stacked five or six deep in the trucks) infuriated Muslim communities in Thailand and worldwide.

So far, the conflict has produced more than 5,000 deaths in the three southernmost provinces. Attacks occur on a daily basis. Successive governments in Bangkok have been preoccupied with ongoing political crisis roughly shaped by the clashes between supporters and enemies of former Prime Minister Thaksin. Violence in the South has been left unattended.

The reasons behind the rekindling of separatism in the South are the combination of economic deprivation of the local Muslim community, political subordination and social discrimination, the rise of Islamism, and an increasing religious intolerance that became part of the Thai state's employment of nationalism to fight against the insurgency.

The Thai state, however, should not solely be condemned for the rise of Buddhist chauvinism. The monastic Sangha and the making of Buddhism as the national religion endorsed by the monarchy all play a role in the monopolization of religious space in Thailand.

For a long time, Thai Muslims have felt alienated and abused. They underwent forced assimilation including the declaration of Thai as the official language. This threatened certain traditional Islamic practices and customs, thereby triggering a violent response from Thai Muslims.

Strife in the South did not only have a bearing on Thailand's domestic politics; there was also an international aspect, especially the impact on Thai-Malaysian relations. Bilateral relations from 2004 onward were mostly influenced by the resurgence of Thai separatism. Thailand's lack of understanding of the conflict and the politicization of the situation generated a rift in Thai-Malaysian relations.

History has justified the role of Malaysia in the southern Thai crisis. The Pattani Kingdom was annexed to Thailand in 1902 prior to the Anglo-Siamese Treaties. Remade as an alien part of a Buddhist-dominated society, the Thai Muslim minority has maintained religious and cultural links with their Muslim fellows in Malaysia. It is known that Malays in Malaysia have been sympathetic toward the plight of the Thai Muslim. Escalating violence at the hands of Thai security forces strained Thai-Malaysian relations.

Until recently, Thai Prime Minister Yingluck Shinawatra had tried to reach out for peace with the Thai Muslim community and for better ties with Malaysia. There were obstacles to the government's efforts. For one thing, local Thai Muslims could not forget what Thaksin did in 2004. And in the political context, the South has never been the territory of the ruling Pheu Thai Party, although the opposition Democrat Party is known to have a position in the South.

Malaysian Defense Minister Hishammuddin Hussein has told the media that he is hopeful of progress through concrete development of Southern provinces: "The issue of development, poverty, fair treatment of everybody — those are the issues to be navigated by both sides based on trust. Building up trust is the difficult part."

Trust will certainly keep alive future negotiations. From a broader perspective, a peaceful Thai South will allow a better Thai-Malaysian relationship.

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