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How much will Chinese flex money muscle?

Stronger yuan promises implications for U.S.

By MICHAEL E. KANELL
Cox News Service

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The jade gates have cracked open, and now it's a question of how wide they will swing

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China said Thursday that it will no longer peg its currency exclusively to the dollar. Instead, the yuan has been revalued slightly and is to be linked each day to a basket of currencies with a cap to prevent it from rising too fast.

The immediate opening was tiny - just a 2% gain in the yuan's value Thursday - but its symbolism was greater. For years, U.S. leaders and manufacturers had complained that hitching the yuan to the dollar gave China an unfair trade advantage; for years, China said it would move the currency in its own time.

Beyond the 2% bump, the yuan is to be allowed to strengthen only in daily increments of no more than 0.3%, with a maximum of 6%.

The Chinese government may halt those increments any time it may pull back the value of the yuan by buying more dollars.

If China keeps a grip on the currency, any long-term effect will be minor. But if the door yawns wide and the yuan grows stronger, that new identity would spread across the global economy, making winners out of losers and losers out of

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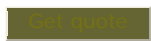
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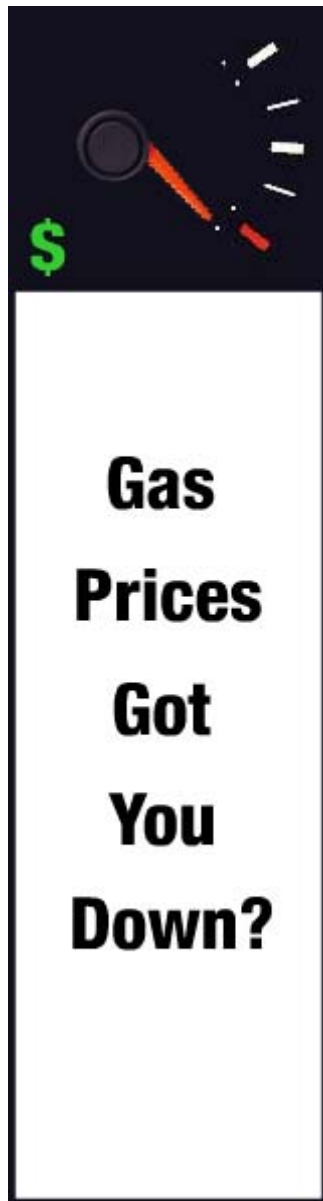
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and reshaping trade in unpredictable ways.

For most people, exchange rates mean little more than how much they pay here for something made by foreign labor - a shirt or car - or how much they pay for a hotel room overseas.

But currency calculations also help set how much our home products fetch overseas, which is why American manufacturers have been wailing for years about the Chinese peg and similar by other Asian countries.

Some U.S. companies benefit from the arrangement. For a stronger yuan and weaker dollar make U.S. goods cheaper overseas - and Chinese goods more costly here.

In a Duke University survey, 15% of companies said a currency change would help them; 11% said it would hurt, "Duke economist Campbell Harvey said.

Still, for manufacturing, the concern is acute.

U.S. manufacturing has lost millions of jobs the past five years in the contest against lower-cost competition.

A stronger yuan makes Chinese products more costly, so when China's currency strengthens, the better the chances to stem manufacturing losses in the United States.

But manufacturing output is up: Many companies have boosted production by using cheaper labor overseas.

The average hourly pay in a Chinese factory is 64 cents, compared with \$21.11 in the U.S., according to Joseph Quinlan, chief strategist for Bank of America's Investment Strategies Group.

"The cost advantage will remain in favor of Chinese manufacturers for some time to come,"

Burl Finkelstein, vice president at Kason Industries in Newnan, Ga., which has contracted Chinese factories to make parts, said that by itself, a currency change can't make up for the costs. "We spend more on our lighting per employee than they spend on labor in China," he said.

Still, with transportation and other operating expenses higher, a currency shift could bring some benefits of sending work overseas, he said. "A significant change would give us a competitive advantage over people who are totally in China, because we could bring work back here," he said.

The sudden change in Chinese policy has spurred concerns about long-term interest rates as those used for mortgages. Those rates have been held down partly by Asian bank purchases of U.S. bonds. China holds nearly \$1 trillion in U.S. securities.

But a stronger yuan might mean fewer dollars in China, which might mean fewer purc U.S. securities. That notion nudged bond prices lower, which sent interest rates up Th

Pessimists worried that it was the start of a trend, and that climbing rates would bring the boom in housing, the economy's most dependable growth engine since 2001.

"The implications for America are enormous," said Peter Schiff, president of Euro Pac Capital in Newport Beach, Calif. "Far from being the panacea that American politician proclaim, China's decision to alter its peg could be the pin that finally pricks America' economy."

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