

Insight not lost on Chinese authorities

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From Prof Stefan Gerlach.

Sir, Martin Wolf (June 18) **correctly notes** that Ben Bernanke sets monetary policy also in China. However, while the quasi-fixed exchange rate of the renminbi may be inappropriate from a macroeconomic perspective, the microeconomic considerations are just as important. Without a full set of liquid derivatives markets to hedge risk, with a lack of modern risk management systems, without a corps of experienced risk management professionals and with many weak banks, a floating exchange rate could trigger widespread financial instability in China. In turn, that would impact adversely on the Asian and the global economy.

That insight is not lost on the authorities, which are gradually increasing the flexibility of the renminbi. While we can argue about the correct speed at which to do so, it is hard to deny that the main problem they face is to balance the macroeconomic benefits of more exchange rate flexibility with the considerable microeconomic risks.

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