South China Morning Post

Now Li Keqiang wants to have his cake and eat it too

Premier pledges to keep mainland growth high amid shakedown of the financial system but may not find it as easy as parrotfish changing sex

By: Tom Holland- July 12, 2013

London mayor Boris Johnson once described Britain's Liberal Democrat politicians as being "like weird hermaphroditic parrotfish, changing sex at will. If they had a policy on cake, they would be pro-having it and pro-eating it".

I don't know about the reproductive habits of parrotfish, but for the rest of it, he could have been talking about China's new leadership.

For the past month or so, the leaders have been broadcasting the message that to prevent a future crisis, China's bloated financial system - where credit has surged to about 200 per cent of gross domestic product - must deleverage, even if that deleveraging means short-term pain and a slowdown in economic growth.

Then after a string of weak data, including Wednesday's dismal trade figures, Premier Li Keqiang turned around and said the government will do whatever it takes to keep growth high to support the labour market.

In other words, Li wants both to have his cake and to eat it: to deleverage the financial system without causing a significant economic slowdown.

It will be neat trick if he can manage it. Unfortunately, he's likely to find it nearly as difficult as changing his sex at will.

Monitor has long been sceptical whether the yuan will win acceptance as a widely used international currency any time soon.

But there are some places where it is rapidly gaining ground as the currency of choice for both government and business.

One is Syria. According to Steve Hanke, who runs the Troubled Currencies Project at Washington's Cato Institute, the government of Syrian President Bashar al-Assad is now conducting all its business in either Iranian rials, Russian roubles or Chinese yuan.

The regime says it has been forced to abandon its own currency by what Deputy Prime Minister for Economic Affairs Qadri Jamil has called an elaborate plot, hatched by the United States and Britain, to "sink the Syrian pound".

Whether Washington and London are really to blame is doubtful. After two years of escalating conflict, the official exchange rate of the Syrian pound has slumped from S£47 to the US dollar to S£103, losing 55 per cent of its value.

That's the official rate. The fall on the black market has been far more severe, with the Syrian pound plunging last month to about S£150 to the dollar.

In an attempt to halt the slide last week, the authorities launched a crackdown on the black market, threatening illegal currency traders with up to 10 years in prison.

As you would expect, the clampdown only accelerated the flight out of the Syrian pound, with the black market value of the currency plunging to S£295 to the dollar (see first chart).

The impact on ordinary Syrians has been brutal.

Hanke calculates that domestic inflation is now running at more than 90 per cent *a month* (see second chart). In other words, prices are doubling every few weeks.

With the government getting access to foreign currency liquidity from its allies in Tehran, Moscow and Beijing, Hanke says the economy in regime-controlled areas continues to function.

But of the three currencies - rial, rouble and yuan - there can be little doubt which both the government and business prefer to hold.

Over the past couple of years the rouble has been weak, falling 15 per cent against the dollar. Officially, the Iranian rial has also fallen 15 per cent, but on the black market it has slumped more than 60 per cent against the dollar.

In contrast, the yuan has strengthened by 6 per cent against the greenback, making it the clear favourite for Assad and his beleaguered regime.

I just wonder whether they are really the sort of users officials in Beijing had in mind when they first launched their currency internationalisation project.