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Hillary Clinton presses China to keep buying US debt

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US Secretary of State Hillary Clinton concluded her weeklong Asian tour Sunday with an explicit appeal to the Beijing government to keep up its purchases of US treasury notes or risk the onset of an even deeper economic crisis engulfing China and the US itself.

On her first overseas trip since being tapped by President Barack Obama, her former rival for the Democratic nomination, as his chief foreign policy representative, Clinton assumed the role of an official high-pressure bond saleswoman.

While the tour also took her to Japan, South Korea and Indonesia, the focus was clearly on economic relations between the US and China.

Her aim was to convince China to keep investing its foreign exchange reserves in US treasury securities in order to help finance the bailout of failing US banks and pay for the $787 billion US stimulus package. The US treasury has indicated it must raise nearly $500 billion in the first quarter of this year alone.

In an interview on China's Dragon TV just before concluding her trip and returning to Washington Sunday, Clinton warned that if the US economy collapsed China would pay a steep price as well. "It would not be in China's interest if we were unable to get our economy moving," she told her interviewer.

"Our economies are so intertwined," she said on the talk show. "The Chinese know that in order to start exporting again to its biggest market … the United States has to take some drastic measures with the stimulus package. We have to incur more debt."

Clinton added, "We are truly going to rise or fall together. By continuing to support American treasury instruments, the Chinese are recognizing our interconnection."

While in her interview Clinton stressed that US treasury bonds are "a good investment, a safe investment," at a joint press conference the day before, China's foreign minister, Yang Jiechi, dodged a question as to whether Beijing would continue buying the US notes, saying only that China would seek safe, high-value and liquid investments for its foreign currency reserves, which at $1.95 trillion are the world's largest.

The Chinese government's policy of buying up US debt has come under increasing criticism from economists within the country. Beijing already holds approximately $700 billion dollars in US treasury bonds, and the critics argue that its exposure is too great and too dangerous given the deep economic crisis in the US and the threat of a dollar depreciation slashing the value of these bonds.

“The rapidly expanding national debt of the US will affect the credit rating for US Treasury bonds,” He Jun, a financial analyst, wrote in China Business News. “US Treasury bonds may become hard pressed to keep their AAA rating.”

He continued: “The US Treasury bond bubble is ballooning and is set to burst. Global investors are keeping a close eye on the mounting risks, but few expect the bubble to explode soon. They are waiting for the best time to dump the bonds. Many of them, however, think that it will be too late to leave the game when China and Japan decide to stop buying or begin selling the US Treasury bonds. China’s financial security is banded tightly with US Treasury bonds, which are fast becoming a risky option.”

Su Chang, a Beijing-based economist with the CEBM consulting group, spelled out China’s dilemma to the AFP news agency: “If it ceased to buy US treasuries, the value of existing holdings of dollar-denominated assets would drop sharply,” he said. “(But) if China continues to buy them, it needs to worry about the possible depreciation of the dollar in future.”

Similarly, Yu Zuyao, an economist at the Chinese Academy of Social Sciences, a government think tank, told the Xinhua news agency, “To rescue the ailing US economy by increasing government borrowing will create a record-high federal deficit. This can further lead to catastrophic consequences such as serious inflation and US dollar depreciation.”

Meanwhile, with some 26 million migrant workers having lost their jobs and 670,000 businesses having shut down because of collapsing export markets for Chinese-made electronics, toys, apparel and other consumer items, there is growing unrest and increasing popular demand that the money be spent at home to alleviate deepening social misery.

China has launched its own $600 billion stimulus package which it must pay for under conditions of sharply decreased tax revenues.

While an 8.8 percent economic growth rate is needed just to generate sufficient jobs for the 24 million new workers who enter the Chinese labor market each year, latest forecasts for 2009 project 5.5 percent growth or worse—down from 11.9 percent in 2007.

Increasingly, government officials are warning that the economic crisis may generate intense social upheavals. According to the People’s Daily, Sun Chunlan, the vice chair of the government-controlled All-China Federation of Trade Unions, warned union bureaucrats and local government officials against the threat posed by mounting unemployment. “Be on guard for hostile forces from both home and abroad that use the problems that businesses are facing to infiltrate and undermine the migrant workforce,” she said.

Clinton made reference to the deepening jobs crisis while defending herself against criticism from human rights groups.

“When you think about the drastic rise in unemployment in China, many would argue that that’s a human rights issue,” she declared. “There’s going to be a lot of suffering that will come from that.”

The US secretary of state deliberately soft-peddled Washington’s habitual criticism of the Chinese regime’s human rights record, insisting that such issues “can’t interfere with the global economic crisis.”

The election of Obama had initially triggered fears in Beijing that the new Democratic administration could pursue a more hard-line policy towards China. During the 2008 election campaign, Clinton herself had argued that China's heavy investment in US debt posed a threat to national security, and she called on Bush to boycott the opening of the Olympics in Beijing to protest China's policy in Tibet and its human rights record.

Yet there was no public criticism from Clinton, even as it was reported that Chinese security forces were placing a number of dissidents in detention or under house arrest for the duration of her visit.

Also absent was any repeat of the recent charges of currency manipulation, voiced less than a month ago by Timothy Geithner during his confirmation hearings as US treasury secretary. Despite this discrete silence on the part of Washington, trade tensions are continuing to mount.

On Monday, just after Clinton left China, a top official in the country's steel industry denounced the "Buy American" provision introduced into the US stimulus package as a violation of rules set by the World Trade Organization. "Such a clause violates the rules of the World Trade Organization," Luo Bingsheng, vice-chairman of China Iron and Steel Association, told China Daily. "It is an act of discrimination against steel products not from only China but other economies, such as Japan, South Korea and Europe."

Despite the evident attempts by Clinton to subordinate all other issues to securing Beijing's agreement to continue purchasing US debt, the objective crisis is rapidly undermining the entire debt-recycling arrangement.

China's role in this process stems from its emergence over the past three decades as the principal cheap-labor platform for corporations from around the world, creating elevated profit rates for them and substantial exchange surpluses for China itself. By recycling its export earnings back into the US, China helped finance the huge US trade and budget deficits, while allowing the maintenance of low interest rates that fueled the housing bubble as well as debt-driven consumption in the US that ensured a market for Chinese-made goods.

The global economic crisis, however, means that far fewer dollars are flowing into China that can then be recycled. Export earnings figures for last month fell by 18 percent compared to a year ago. Even more ominous, imports, much of which consist of parts and materials for manufacturing, plummeted by 43 percent, a figure that foreshadows even steeper declines still to come.