Corona calamity: The role of China's cheerleaders

By including the yuan in its basket of leading currencies, the IMF gave China a legitimacy it did not deserve

As the count of coronavirus cases and fatalities mount, and the economic catastrophe worsens, one should step back to examine all of those who bear some responsibility for this grave calamity. The cover-up by Chinese officials — who forced the whistleblowing martyr doctor Li Wenliang to sign a retraction in early January — has justifiably led to scathing criticism of the Chinese government and tributes to him.

A careful examination of the steps taken by the World Health Organization (WHO) and other supra-national bodies after the SARS epidemic of 2003 originating in Guangdong to pressurise China to clamp down on its wet meat (live animal) markets is also called for. Further, was the WHO sufficiently proactive after it was informed on December 30, 2019, by the Chinese government about the virus? These questions need to be examined threadbare by medical experts in the months ahead. This article is to highlight China's long-standing dubious economic practices and to point to its "cheerleaders".

The International Monetary Fund (IMF) should be singled out for being such a cheerleader. When the Bretton Woods system-fixed exchange rates administered by the IMF collapsed in 1971, one of its main tasks became to promote the Special Drawing Right (SDR). The SDR was the "currency" created by the IMF to both supplement and supplant the US dollar for international transactions.

The SDR comprises a basket of leading currencies based on two criteria: (i) The country must be one of the five leading exporters in the world; and (ii) the currency must be freely usable. In November 2015, as part of its periodic review, the IMF decided to include the yuan in its SDR basket, the other four currencies being the US dollar, the euro, the Japanese yen and the pound sterling. China met the first criterion hands down, being the world's largest exporter for many years. However, it failed to meet the second criterion — that its currency must be freely usable. The IMF decision to include the yuan, effective October 2016, was made even after China's stock market tumbled in August 2015 and it imposed sweeping restrictions on its resident and overseas investors, blatantly violating the freely usable criterion.

The inclusion of the yuan in the SDR basket has been a more symbolic than substantive event since the SDR is barely used for payments. Nevertheless, by doing so, the IMF accorded China a legitimacy it does not deserve, thereby incentivising its government to continue with its autocratic ways.

The IMF apart, Arvind Subramanian (former chief economic advisor to the Government of India and earlier a senior IMF official) has also been a cheerleader of China. In his 2011 book, *Eclipse: Living in the Shadow of China's Economic Dominance*, he wrote: "First, the economic dominance of China relative to the United States... will be more broad-based... the fundamentals will be in place to facilitate the rise of the renminbi and its eclipsing of the status quo reserve currencies, the dollar and the euro".

This prediction was derived from models of the demand for a reserve currency, building on projections rooted in the convergence and the gravity models of growth and trade respectively. In critiquing his conclusion, I wrote, "...despite the yuan entering the SDR basket... due to the growing crisis in the Chinese economy, and other considerations, such an outcome is very unlikely" (*Applied Macroecon-omics*, 2017, page 143).

As per the IMF data for 2019, the share of US dollar (62 per cent), euro, yen and sterling in global FX reserves was a combined 92 per cent. Thus the yuan's share could at most be 8 per cent, and probably around 5 per cent. To paraphrase Mark Tawin about his own demise, the predictions of the demise of the dollar have been greatly exaggerated.

Regarding economic dominance, as distinct from the currency's importance, it is well known that due to a flawed incentive structure, China's provincial governments puff up their GDP data. Subramanian deals with the data quality issue and discusses the estimates of Nicholas Lardy, a critic of pessimistic projections of China's growth prospects. However, he ignores the harsher critics of its data — notably, China's GDP expert Thomas Rawski at Pittsburgh University, and then Hong Kong-based critics of its data — notably Harry Wu and Karsten Holz.

Indeed, the Standard Chartered Bank index based on industrial goods production, freight, bank credit and major imports created by Stephen Green indicated that China's output was vastly lower than official estimates. As Green put it, back in the 1990s itself, Beijing was said to be "adding water", a Chinese euphemism, to its GDP. ("Lies, Damned Lies and Chinese Statistics", *Far Eastern Economic Review*, January/February 2009).

Going beyond GDP to human life, an infinitely more important matter. It is well known that the SARS epidemic, which started in Guangdong in November 2002, was initially hushed up by provincial officials. The accuracy of quarterly GDP estimates for 2003 were discussed by Rawski in SARS and China's economy in 2005. There is no mention in this book, *Eclipse,* of SARS, a glaring omission, let alone an assessment of China's capacity to be the world's leading economy without free speech.

Subramanian's failure to provide an objective assessment of China's economy is particularly noteworthy since last year at Harvard University he used raw data proxies (as Green did for China, documented above) to show that India's growth was hugely overstated. I hold no brief for the recent manipulation of Indian data that started in January 2015. However, I leave it to the reader to judge whether it is fair to project China's economic dominance based on its dubious data while criticising those of India much later.

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