

At its own pace

Yang Tao believes that China will increase the flexibility of the renminbi exchange rate and eventually peg it to a basket of currencies – but only gradually, and in step with the needs of its economy

Different from most countries, China's exchange rate policy is not determined by the Ministry of Finance, but is developed by the state and implemented by the State Administration of Foreign Exchange under the central bank. Of course, as with other domestic monetary policies, the central bank does not have the power to dictate the policy, given the enormous influence of the central government.

Three factors are believed to influence Beijing's attitude towards the exchange rate policy. The first is its influence on exports. The large price elasticity for exported goods means any appreciation of the renminbi may result in rising production costs, which will damage labour-intensive industries. Furthermore, due to the low levels of profitability for exporters of hi-tech products, and the low proportion of independent domestic research and development, these exporters are also vulnerable to exchange rate fluctuations.

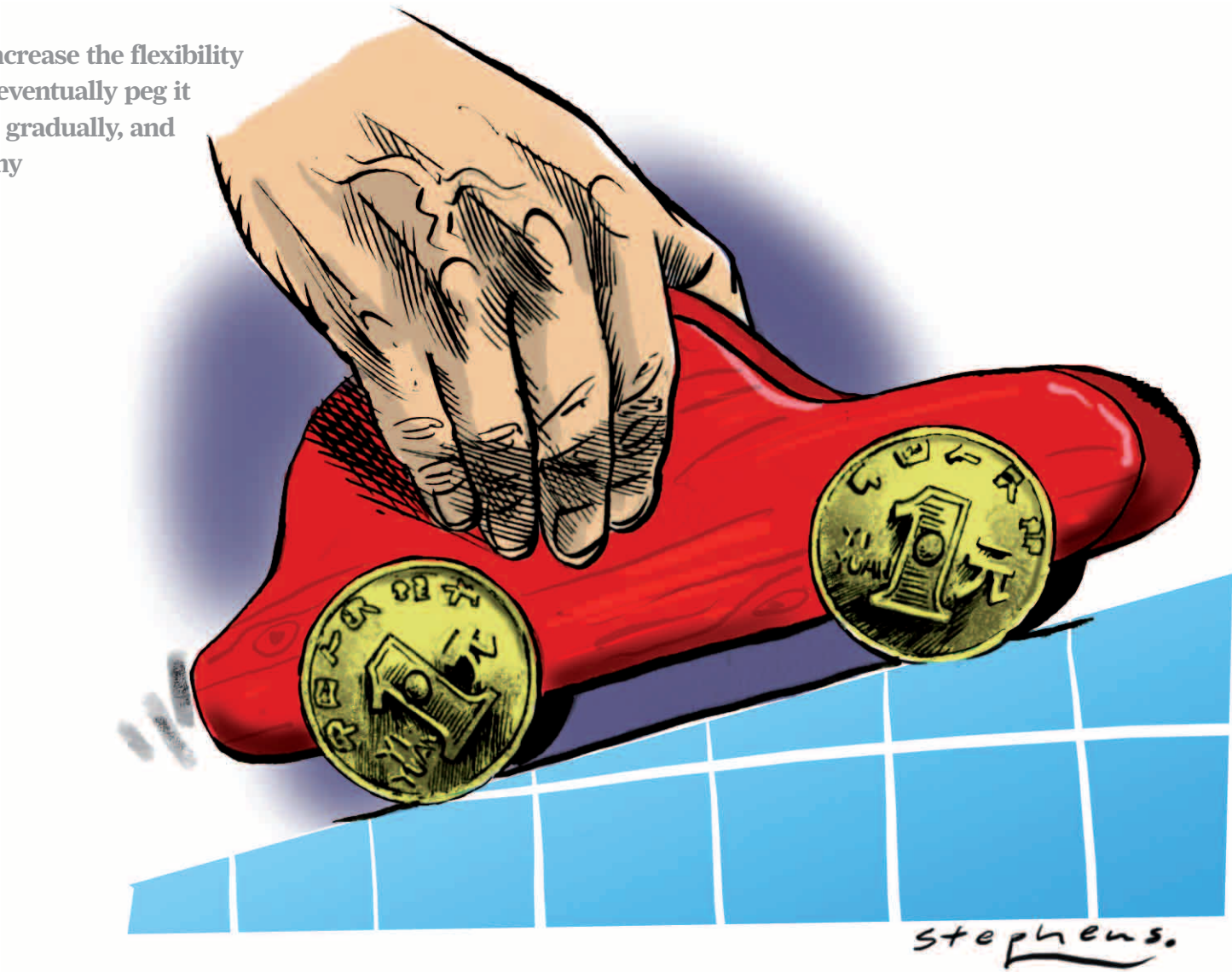
Then there is the impact of the policy on domestic financial operations. The involvement of speculative investment funds in previous national and international financial crises has caused many senior government leaders to be especially sensitive to financial risks, including those related to international "hot money".

It is generally accepted that the expected appreciation of the renminbi, and the difference in interest rates between China and developed economies such as the US, would lead to the arbitrage of interest and exchange rates using hot money. If hot money is directly invested in China's property or stock markets, rather than introduced in the form of loans, the expected yields would attract a significant quantity of foreign investment. When the renminbi appreciates to the target price, investors would convert their assets into foreign currencies and leave China. Thus, the inflow of hot money would bring asset bubbles and inflation risks, and affect the country's economic security and financial stability.

International investors generally believe Beijing has strict control over exchange rates, so if there is a rapid appreciation, it would typically be viewed as an expression of the government's long-term approach. This wouldn't reduce expectations of renminbi appreciation; instead, it would raise the risk of hot money inflows.

Finally, there's international political negotiations. To a large extent, the renminbi exchange rate has become a bargaining chip in negotiations between China and the US. Although both sides understand renminbi appreciation will not change their trade structure, there is a tacit understanding that they are playing a negotiating game.

Economist Paul Krugman has cited the Mundell-Fleming theory of the "eternal trian-



gle", which states that free capital flows, an independent monetary policy and fixed exchange rates cannot all be achieved at the same time. The practice of China's exchange rate policy in recent years has been to maintain independent monetary policy and limited capital flows by allowing a gradual increase in exchange rate fluctuations.

It is foreseeable that the authorities will reconcile their attitudes towards the exchange rate policy. The government will become more tolerant towards the marketisation of the rate, and the central bank will allow a gradual appreciation of the renminbi. Specifically, I believe the compromise will develop as follows:

First, the trend of gradual appreciation will not be altered, but its speed will increase during the 12th five-year plan. Although many scholars

China and the United States should seek to resolve their conflicts so that both sides gain

have argued in favour of a significant appreciation, and a one-off appreciation, these positions do not reflect mainstream thinking among decision-makers. Because gradual reform can reduce costs and the responsibilities of decision-makers, such a policy is more in step with the characteristics of China's reforms. No one is willing to take responsibility for more drastic action.

Second, exchange rate flexibility will be further improved. The range of the "managed float" may be increased. Due to the limited floating rate of the renminbi against the US dollar, the central bank has been forced to become the largest buyer of US dollars in the foreign exchange market in order to have an impact on the price. This resulted in multiple contradictions, such as the large quantity of foreign exchange reserves held by the central bank, significant domestic inflation pressure caused by outstanding funds being used for foreign exchange, and the high costs for hedging currency. To some extent, the central bank will increase exchange rate flexibility in the hope of reducing such costs.

Third, there will be an improvement in the exchange rate formation mechanism. China's foreign exchange market is too small; it lacks

foreign currency financial products, and cannot truly have a role in price discovery. These factors promote the innovation of foreign exchange products. As a result, increasing the size of transactions and becoming an important market participant have become reform goals. Therefore, reform of the exchange rate formation mechanism, basing it on a basket of currencies, is likely to be initiated.

It is worth noting that the current reforms and modest appreciation of the renminbi exchange rate have been a result of changes in the size and structure of China's economy. External pressure from the US and other developed countries may have a positive impact on the rate in the short term. But, in the long run, it would cause conservative ideas to dominate, which would work against the marketisation of the exchange rate. Therefore, China and the US should seek to resolve their conflicts so that both sides gain, rather than using the exchange rate as leverage in a game where, if one party wins, the other must lose.

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Out of step

Michael Chugani says our top bureaucrats need to put themselves in the people's shoes to tackle a problem, be it vote-rigging or fire risk



At first they brushed it off as sour grapes. Chief Executive Donald Tsang Yam-kuen didn't even bother to mince words. Sore losers whining – that was essentially what he said. But, day by day, the media uncovered more and more cases of suspected voter fraud in last month's district council elections. A trickle turned into a flood. By the last count, there were some 800 cases of suspected irregularities.

Is it the tip of an iceberg of massive vote-rigging? It's too early to say. But it's not too early to ask if the election outcome was legitimate, or if we're heading for a confidence crisis over our election process. Concern, however, doesn't appear evident among our top officials. Denial does.

That was underlined by the monotone response of Chief Secretary Stephen Lam Sui-lung last week when it emerged that the Audit Commission had identified voter registration loopholes back in 2006. Lam wouldn't admit the system is flawed. Rather, he said the commission's concerns had been dealt with.

If they were, how come the latest election still produced hundreds of suspected vote-rigging cases? In fact, as the audit commissioner noted, the government had ignored some of his key 2006 recommendations that would have tightened the voter registration system against fraud.

Lam's dismissive demeanour, though distressing, did not surprise me. It is endemic of our top bureaucrats. They see things not as people but as bureaucrats. Former security secretary Regina Ip Lau Suk-ye, now a legislator, has admitted as much, describing our bureaucrats as living in a cloistered world of their own.

That is why they could not sense the public's alarm when the media revealed the first cases of suspected voter fraud. That is why, when fire swept through the maze of market stalls in Fa Yuen Street a year ago, officials could not sense the fear among district politicians and residents that another inferno was waiting to happen, as it did last week.

After last week's tragedy, officials mouthed their usual mantra that they had taken all the necessary steps to prevent a repeat following last year's fire, just like Lam had insisted all steps were taken in 2006 to prevent voter fraud. Yet vote-rigging did occur, as did a repeat of the Fa Yuen fire.

It is, of course, impossible to make voting foolproof against fraud or a place completely fireproof. But the vote-rigging and last week's suspected arson were so preventable that we did not require a foolproof system to prevent them.

Our bureaucrats probably did take all the steps they thought necessary; they implemented bureaucratic solutions. How could they do otherwise when they see the maze of market stalls, sub-divided flats and blocked stairwells as a bureaucratic problem to be dealt with, not a problem involving people?

I attended a recent function where the guest of honour was a top bureaucrat. He arrived with his handlers, strode on stage, said his stuff, engaged in a few minutes of small talk with his hosts and then abruptly left, surrounded by his handlers. The ordinary people in the room were invisible to him. Even the president of the United States doesn't behave so haughtily.

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Where's the political will to help parents with childcare?

Julian Groves says it is too easy to make an issue of foreign domestic helpers

Members of the Civic Party were probably right to question legislation regarding the right of abode for migrant domestic helpers. We should scrutinise laws that look discriminatory, regardless of whether or not it is politically savvy to do so. But the party that gets my vote will be the one that proposes affordable childcare solutions for working mothers. Isn't that the elephant in the room that no one wants to talk about in the tiresome debates about migrant domestic helpers?

We should not be surprised that there is almost no viable alternative to affordable childcare in Hong Kong other than to hire migrant workers. Women make up less than 20 per cent of the Hong Kong government. If the government was comprised of 80 per cent women and 20 per cent men (compared to the other way around), would there be more political will to provide affordable childcare for working parents? Or imagine a world in which only men could biologically bear children. Would there be the shortage of hospital beds and midwives to assist with childbirth that we have at the moment?

In the 1980s, the government assisted migrant domestic helpers in their bid to come to Hong Kong because Hong Kong residents needed them: for childcare, housework and to care for elderly parents. In Britain, where I grew up, the government similarly imported migrants from former colonies in the 1950s to fill a growing demand

for cheap unskilled labour. They learned the same lessons about immigration that Hong Kong residents are learning now. There will be costs and inconveniences. You can't have your cake and eat it.

Domestic helpers do not pay tax. But they do provide welfare. If the Social Welfare Department were to pick up the bill for the childcare, housework and care of elderly family members that these helpers now undertake, I doubt that the government could boast of the economic surplus that it currently enjoys. To say that helpers contribute little towards the economy, as some claim, hangs on a very narrow definition of economic productivity indeed.

For every tax-paying working mother in the workforce today, there is a probably a migrant domestic helper picking up her children from school and preparing meals at home. Statistics suggest that men certainly aren't doing it. Women alone continue to do most the regular housework and childcare.

Further, the proportion of our population over the age of 65 has risen sharply in the past 20 years and will continue to do so. Who will be taking care of them?

Above the cacophony surrounding the right of abode, it should be obvious that we treat domestic helpers differently because they do women's work in a society in which women's contributions are at best undervalued, and, at worst, rendered invisible. If the Equal Opportunities Commission was serious about promoting

opportunities for women in Hong Kong, it should be vigorously supporting both domestic helpers and their employers. Why don't we hear from them on this issue?

It is of course understandable that, since Hong Kong's return to China, Hong Kong residents worry that the unique way of life that they have enjoyed in this city might be submerged by uncontrolled immigration and the inevitable tide of globalisation. I worry about that, too. But anyone who sincerely cares about livelihood issues in Hong Kong has far more to fear from, say, wealthy mainlanders and greedy property developers buying up affordable housing and doubling rents so that small businesses can't survive, than the peaceful assemblage of nannies in the park. Poor women make easier targets than those behind these more sinister commercial interests.

It is intellectually easy and politically expedient to ruminate about migrants, rights, resources, entitlement and so on. When it comes to childcare, however, everyone likes a party, but nobody wants to clean.

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No meritocracy without equal chances for all

Pranab Bardhan says democratic societies must invest in education for the poor and infrastructure

Inequality is on the public's mind everywhere nowadays. Indeed, in the world's two largest democracies, India and the US, popular movements against rising inequality and elite greed are becoming salient issues in looming national elections.

In both countries, some social inequalities have been on the decline over the past few decades. These developments reflect a democratic advance. But, at the same time, the fabric of democracy is being torn apart by a staggering rise in economic inequality.

A fundamental tenet of American society is that everyone has an equal chance. In India, there is a general feeling, shared even by some of the poor, that the rich deserve their wealth because of their merit, education and skills. There are two problems with this argument. First, education and skills are not inborn talents. The rich have access to better schools, health care, nutrition and social support than the poor, which plays a decisive part in success.

The other problem is the rising importance of "unearned incomes". In India, scarce public resources such as land, oil and gas, and telecommunication spectrum have shot up in market value, generating high unearned income for the politically well-connected.

In the US, the deregulation of the financial sector, and the accompanying rise of dubious financial instruments, destabilised the real economy. The result, as everyone knows, was exorbitant

financial gain for a select few, followed by large losses that were paid for by the many.

In democratic societies, groups that promote social discrimination grow politically weaker over time. Economic inequality, on the other hand, is perpetuated through the politically powerful and well-funded lobbies of the rich.

This implies that the egalitarian movements need to broaden their focus to include, among other things, an overhaul of the education system to ensure high-quality schools for the poor. In addition, massive investment in both countries' creaking physical infrastructure would create jobs.

The question is why India and the US neglect both education for the poor and infrastructure. The answer lies partly in the fact that the rich in both countries are ceasing to use many public services, making it increasingly challenging to tax them to pay for services they do not want or need.

The world's two largest democracies must find a way to channel the rising anger caused by economic inequality into productive investments that make the rich feel that they have a stake in ameliorating conditions for the poor. If India and the US move towards overcoming the most pervasive inequality of all, they will reinvigorate their democracies – and their economies.

Pranab Bardhan is author of *Awakening Giants, Feet of Clay: Assessing the Rise of China and India*

A rational approach to personalised medicine

Henry Miller urges sensible control of drugs that promise higher efficacy, with fewer side effects

Over the past decades, treatment for a variety of conditions has begun to shift from a "one size fits all" approach to a more personalised strategy. As a result, patients can more often be matched to the best drug for their genetic makeup or the subcategory of their disease. This enables physicians to avoid prescribing a medication that might cause serious side effects.

In other words, even among patients who apparently have the same disease and symptoms, the treatment for each one would be determined by various predictive or prognostic tests. But, while this hi-tech approach could be a boon to patients, it could prove detrimental to drug companies' bottom lines. The reasons are subtle.

Personalised drug therapy uses biological indicators, or "biomarkers" – such as DNA sequences – as an indicator of how patients should be treated.

In cancer therapy, drugs such as Erbitux and Vectibix work only in tumours containing the normal version of a gene called Kras. If mutations are present, the drugs are ineffective. Information about a patient's genes will sharply reduce the number who are unnecessarily subjected to the side effects (and expense) of drugs that will not work.

Improving the efficacy and reducing the side effects of drug therapy will be a boon to doctors, patients and insurance companies, to be sure, but why should

pharmaceutical companies embrace personalised medicine?

The presence of biomarkers will enable drug companies to perform smaller, better-targeted clinical studies. Thus, when drugs are ultimately approved based on the use of biomarkers, the description of the medication's approved uses, which is printed on the label, might be more restrictive – that is, it might reduce the size of the patient population for which the drug is intended.

In reality, however, the situation is more complex. Even if smaller, better-targeted clinical trials offer clear evidence of a drug's efficacy, regulators might demand far larger studies to provide evidence of safety. Increasingly, regulators have in recent years required massive, hugely expensive, and time-consuming clinical trials designed to detect even very rare side effects.

Thus, the impact of personalised medicine in the short term might be positive at the patient's bedside, but vast clinical trials to demonstrate the safety of new drugs will impose huge costs that manufacturers might never recover.

If society is to derive the maximum benefit from personalised medicine, regulators will need to adopt reasoned and reasonable policies.

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