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DEPARTMENT OF THE TREASURY  
REPORT TO THE CONGRESS  
ON  
INTERNATIONAL ECONOMIC AND EXCHANGE RATE POLICY  
MAY 1992

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## PART I: INTRODUCTION

Section 3005 of the Omnibus Trade and Competitiveness Act of 1988 (Pub. L. 100-418) requires the Secretary of the Treasury to submit to the Committee on Banking, Housing, and Urban Affairs of the Senate and the Committee on Banking, Finance and Urban Affairs of the House of Representatives an annual report each October 15 on international economic policy, including exchange rate policy. In addition, Section 3005 requires that the Secretary shall provide a written update of developments six months after the initial report. Annual reports, pursuant to Section 3005, have been submitted since 1988. This is the fourth update of developments to be submitted to Congress.

Part II of this report reviews the economic situation in the industrial countries and efforts by major countries to coordinate economic policies. Part III analyzes developments in the foreign exchange markets, including the dollar's movement relative to the currencies of major trading partners and U.S. foreign exchange market intervention. Part IV examines the U.S. balance of payments situation and related economic issues. Part V, prepared pursuant to Section 3004 of the Omnibus Trade and Competitiveness Act of 1988, considers whether countries manipulate the rate of exchange between their currencies and the U.S. dollar within the meaning of the legislation. In this connection, the report reviews and assesses developments and policies in Taiwan, Korea, and China. The final chapter provides conclusions on the principal issues discussed in the report.

PART II: ECONOMIC POLICY COORDINATION  
AND THE ECONOMIC SITUATION IN THE INDUSTRIAL COUNTRIES

Since the mid-1980s, the Group of Seven (G-7) has worked intensively to achieve consistent and compatible policies and performance necessary for sustained growth with price stability, reduced external imbalances and greater stability of exchange markets. The economic policy coordination process grew directly out of each country's growing recognition that, in an interdependent world, economic performance at home depends in large part on economic developments in the rest of the world, and particularly in the major industrial economies.

As recent experience has once again demonstrated, the formulation of economic policies -- especially fiscal and monetary policies -- by individual G-7 countries has a major impact on the economies of the others. Moreover, no individual G-7 member acting alone can overcome economic difficulties which affect all of the G-7 economies.

The G-7 record in the second half of the 1980s was one of success on a broad range of objectives. The G-7 countries achieved the longest peacetime expansion on record in the context of lower inflation, reductions in external imbalances, and more stable exchange markets. In addition, as the usefulness of the G-7 process became increasingly evident, it was expanded to cover a wide range of important international economic issues as they emerged.

Beginning in 1991 and continuing into 1992, the G-7 Finance Ministers and Central Bank Governors have confronted two major challenges: a growth slowdown in their own economies and the need to foster a global environment which supports sweeping economic reforms in Latin America, Eastern Europe, and the new states of the former Soviet Union.

Below is a description of the current economic situation and prospects in the major countries, and the G-7's response. (See Table 1.)

Growth

This year, on an aggregate basis, the major industrial countries are experiencing their third straight year of substandard growth.

After the G-7 slowdown in 1990, growth in 1991 was the slowest in a decade. Aggregate GDP/GNP growth in the major industrial countries (includes eastern Germany) fell to 0.8 percent in 1991, from 2.5 percent in 1990. The worst growth quarter in 1991 was the fourth, when aggregate G-7 output was flat.

Within the G-7, growth patterns in 1991 diverged at the beginning of the year, but by year-end, slow growth was being recorded throughout the group. The United States, Canada, and the United Kingdom were in recession as the year began. They recovered slightly in the middle of the year, but faltered again in the fourth quarter.

By contrast, western Germany and Japan began 1991 with strong growth. But as the year progressed their growth slowed, to the point that both countries suffered output declines in the fourth quarter. Finally, in France and Italy growth also slowed in the second half of the year, influenced by developments in Germany.

For the G-7 as a whole, the IMF expects 1992 growth at around 1.7 percent. While signs of recovery are emerging in the United States and Canada, these recoveries are expected to be modest, particularly in comparison with historical averages. Meanwhile, annual average growth is slowing in Germany and Japan and remains modest in other European countries.

Growth trends in Europe are being heavily influenced by developments in Germany. In the past years, German fiscal deficits have risen sharply as a result of substantial spending increases associated with reunification. These deficits are projected by the IMF to remain large in the coming years. Moreover, unlike in the rest of the G-7 (see below), German inflation on an annual average basis is projected to rise in 1992 (after rising in 1991), and lately there have been substantial wage pressures. As a consequence, German monetary authorities have raised official interest rates, the latest such increase in December 1991. These higher interest rates have in turn spilled over into the rest of Europe, dampening growth and growth prospects.

In Japan, 1992 growth is expected to fall by half (from 4.5 to 2.2 percent) from 1991. The slowdown is in part associated with the tightening of monetary policies from 1989 to 1991 in an effort to brake price increases, and in particular, asset price inflation. Recent cuts in interest rates, however, should moderate the slowdown in growth. Meanwhile, Japan's fiscal position remains strong. The IMF estimates that Japan's general government fiscal surplus is on the order of 3 percent of GNP.

Growth is recovering in the United States and Canada. Indeed, the IMF projects that the fastest growing G-7 economy will be Canada, albeit at a modest 2.3 percent. Factors which will contribute to recovery in the United States and Canada include lower short-term interest rates associated with significant declines in inflation. In addition, households and firms have reduced their debts. Nevertheless, these projected recoveries are quite weak by historical standards.

### Price Trends

Price trends in the G-7 countries, in contrast, are encouraging, and further substantial improvement is expected.

In 1991, G-7 (excluding eastern Germany) consumer price inflation fell to 4.2 percent, from 4.8 percent in 1990. This improvement reflected the decline in oil prices early in the year in the wake of the Gulf hostilities as well as the more moderate pace of economic activity. Among the G-7 countries in 1991, France had the lowest inflation rate, at 3.1 percent, and surpassed its long-standing goal of reducing its inflation to the level of German inflation. The United Kingdom showed the most improvement in 1991, as inflation fell to 5.9 percent from 9.5 percent the year before. The only G-7 country to show a significant rise in inflation was (western) Germany, where the rate rose to 3.5 percent, from 2.7 percent in 1990.

For 1992, the IMF expects aggregate G-7 inflation to fall sharply further to 3.1 percent. Apart from the period from 1986 to 1988, when inflation was even lower due to the 1986 oil price decline, the anticipated 1992 inflation rate would be the lowest since 1967.

The decline in inflation is expected to be shared by all countries, except Germany. U.S. inflation is projected to be in line with the G-7 average. Meanwhile, Canada is expected to have the lowest inflation, 1.7 percent, followed closely by Japan at 2.2 percent. For Canada, this outcome would represent a major improvement over 1991, when inflation rates were pushed up by the January inauguration of the Goods and Services Tax. Also U.K. inflation is expected to register a further major decline. In contrast, (western) German inflation is expected to rise to 3.8 percent.

### External Account Developments

External account developments reflect continued reduction in the U.S. trade deficit, continuation of the German deficits, and further sharp increases in Japan's already large external surpluses. Since 1987, when U.S. trade and current account deficits peaked, over 60 percent of the deterioration in the U.S. external position of the early 1980s has been reversed. This reversal has been associated with strong and continuing gains in U.S. competitiveness. (For a discussion of this issue and its implications for the U.S. economy, see Part IV.)

In 1991, external imbalances of several large G-7 countries narrowed in dramatic fashion. The U.S. current account deficit fell from \$92.1 billion to only \$8.6 billion, while Germany's \$47.9 billion current account surplus shifted to a \$20.6 billion deficit. Two other countries, Canada and Italy, suffered modest deterioration in their current account deficits. By way of contrast, Japan's current account surplus doubled, from an already large \$35.8 billion to \$72.6 billion.

The sharp reduction in the U.S. current account deficit last year was related to three major factors: oil import prices fell (by about \$2.44 per barrel between 1990 and 1991); one-time transfers in support of Desert Storm, totalling \$42.4 billion, were received; and the U.S. recession induced stagnation in import growth. While none of these special factors will recur this year, strong export growth, import moderation, and a strong services balance are likely to underpin further underlying improvement in the current account position. (These developments are discussed further in Part IV.)

For (unified) Germany, reunification led to a sharp rise in domestic demand in the east that (along with Desert Storm associated transfers) erased the long-standing German surplus. The shift from surplus to deficit continued until growth slowed in the second quarter of 1991. Shortly thereafter, the deficit seemed to stabilize; current forecasts of the deficit are in the \$10 to \$15 billion range for 1992.

But Japan's external surplus is large and growing, and it is projected to exceed \$90 billion in 1992 and remain very high thereafter. On a geographic basis, most of the rise in Japan's trade and current account surpluses has been accounted for by higher bilateral surpluses with Europe and East Asia; Japan's trade surplus with the United States rose by only \$2.4 billion. Japan notes that its current account surplus now represents only some 2 percent of GNP, down from its surplus in the range of 4 percent in 1986-87. Nevertheless, the sharp rise in Japan's already large surplus is a matter of systemic concern.

#### The G-7 Response

Early in 1991, the United States recognized the risks inherent in the economic outlook, particularly for world growth, and urged the adoption of policies consistent with the shift in the balance of risks towards low growth. Since this time, these views on world growth have been borne out. In spring 1991, the IMF projected real G-7 growth of 1.3 percent in 1991 and 2.9 percent in 1992. As noted, G-7 growth in 1991 was only 0.8 percent, and in its latest projection, the IMF forecast much lower 1992 G-7 growth of 1.7 percent.

In meetings with European officials in April 1991 and in the June 1991 G-7 meeting, Secretary Brady stressed the need to forge a growth-oriented policy strategy, building on the substantial gains made in reducing G-7 inflation. In these meetings, the United States emphasized that the importance of such a strategy extends beyond improving the performance of G-7 economies themselves. It can create a global environment that supports the struggle to create market economies in the new states of the former Soviet Union and in Eastern Europe; and it can help facilitate the economic reform process in Latin America and in parts of Africa and Asia.

In light of increasing concern about the timing and strength of economic recovery, in January 1992 the G-7 Finance Ministers and Central Bank Governors agreed to intensify cooperative efforts to strengthen world economic growth. At the January meeting, each government set out specific economic policy objectives geared to improving economic performance.

At the April G-7 meeting, participants noted the emergence of signs of recovery in some of the G-7 countries. They also noted additional positive signs: significant declines in inflation in most of the G-7 countries; substantial cuts in short-term interest rates in some of G-7 countries; reductions in consumer and business indebtedness problems; and falling external imbalances in most G-7 countries. But they remained concerned that overall aggregate G-7 growth would be inadequate for 1992, with adverse implications for reducing unemployment and meeting the challenges presented by reform movements in much of the rest of the world.

Against this background, they agreed that all countries with large budget deficits should pursue credible medium-term fiscal consolidation in order to create the basis for lower real interest rates and reduce government demands on private savings to facilitate needed capital spending. Countries with large fiscal deficits, relatively high inflation, excessive wage developments and tight monetary policy should follow a balanced policy approach to facilitate improved growth. They agreed that, in other countries, with large surpluses and declining growth, policymakers should be mindful of the possibilities of strengthening domestic demand through appropriate measures.

The G-7 also stressed the need for vigorous structural reforms which can make a considerable contribution to growth. Reductions in subsidies, labor market rigidities, and trade barriers promote better resource allocation, greater efficiency, and growth without inflation. In this regard, the Ministers and Governors reemphasized the importance of bringing the Uruguay Round to a rapid and successful conclusion.



### PART III: DEVELOPMENTS IN FOREIGN EXCHANGE MARKETS

#### Overview

Since the fall 1991 report the dollar has, on balance, moved narrowly against most major currencies, continuing to reflect generally stable exchange market conditions. The yen weakened somewhat over the period, while the dollar appreciated steadily against the Canadian dollar. On a real trade-weighted basis, the dollar has also showed little net movement. Interest rate considerations related to cyclical economic developments were the primary factor in exchange rate fluctuations over the period. (See Table 2 and chart on real trade-weighted exchange rates.)

G-7 economic cooperation contributed to the relative stability of exchange markets over the period. At their April meeting, the G-7 Ministers and Governors noted the general stability of markets and reaffirmed their commitment to close cooperation in exchange markets, which can contribute to facilitating recovery. They also noted that the recent decline in the yen was not contributing to the adjustment process.

#### Fall 1991: Dollar Decline

Slower than expected U.S. economic growth in the fall of 1991 caused the dollar to depreciate through the end of the year. The dollar moved steadily lower as the Federal Reserve eased reserve market conditions in response to slowing economic growth and sluggish growth of M2 and M3 monetary aggregates. Market participants judged inflation to be at low enough levels to allow room for additional reductions in interest rates, adding to downward pressure on the dollar. A sharp decline in U.S. equities prices in late November also contributed to the dollar's depreciation.

The dollar declined most sharply versus the mark. While U.S. rates fell, German monetary policy tightened and German interest rates rose relative to those of the United States. In mid-December, the German central bank hiked its key short-term interest rate (Lombard) from 9.25 percent to 9.75 percent and its official discount rate from 7.50 percent to 8.00 percent. At the same time the Federal Reserve was cutting its target for the Federal funds rate from 4.5 percent to 4.0 percent. At end year, the dollar was at its lowest levels (DM 1.5015) since just before the outbreak of hostilities in the Gulf in February 1991, and only moderately above post-war lows against the mark (DM 1.4433).

The dollar declined less against the yen due to moderating economic growth in Japan, which stimulated expectations that Japanese interest rates would also decline. The Bank of Japan started easing monetary policy in the summer of 1991, and it has since cut its official discount rate four times (from 6.0 percent to 3.75 percent) in an effort to revive economic activity. As a result, Japanese interest rates declined slightly vis-a-vis those of the United States during this period.

However, downward pressure on the dollar versus the yen was generated by sentiment among foreign exchange traders that U.S. and Japanese authorities might implement measures to strengthen the yen, to combat the growing Japanese trade surpluses. Japanese officials repeatedly called for a steady appreciation of the yen. Concern over a coordinated effort to increase the value of the yen heightened prior to and during President Bush's trip to Asia.

These expectations waned somewhat when a joint statement by President Bush and Prime Minister Miyazawa concluded that "recent exchange movements were consistent with current economic developments." But in mid-January, the dollar declined in response to purchases of yen by U.S. and Japanese authorities. By mid-January, slowing U.S. economic growth and fear of central bank intervention combined to send the yen briefly under ¥ 123 for the first time in over three years.

#### Winter to Mid-March 1992: Dollar Rebound

The dollar rebounded sharply starting in late January 1992, largely based on market expectations of an economic recovery in the United States and slowing growth in Germany and Japan. Sentiment regarding the U.S. economy turned more positive in early January, as traders anticipated a cyclical rebound in economy activity. The larger than predicted employment gains in December and February and strong retail sales in January and February were the most important factors in this regard.

Yen weakness also emerged in this period. The yen was weakened by political and financial scandals and sagging Japanese equity prices. Also, the Bank of Japan continued to ease monetary policy as it appeared that Japanese economic growth was much weaker than previously expected. However, dollar appreciation versus the yen was slowed by reports of intervention by Japanese authorities, with more limited participation by U.S. authorities, in mid-February and early March. Japanese officials repeatedly expressed displeasure with the dollar's rise, fueling concerns that the G-7 countries opposed strong depreciation of the yen.

The dollar's upward momentum against the mark was strengthened by the possibility of strikes in Germany and by fear of political and economic instability in Eastern Europe and the former states of the Soviet Union.

Mid-March to Mid-April

The dollar's appreciation paused from mid-March through mid-April. Despite signs of reviving economic activity in the United States, exchange traders remained cautious about buying dollars until unambiguous signs of a strong rebound emerged. Slowing U.S. money supply growth and only modest gains in some other economic indicators added to traders' caution.

Moreover, market participants judged that German interest rates were more likely to rise than fall. These perceptions were fuelled by statements from German monetary officials indicating that there was little prospect of an interest rate reduction in the near term, because of high money supply growth, high bank lending levels, and high budget deficits.

The U.S. dollar appreciated against the Canadian dollar from the last report until late March, partly as exchange market participants responded to slower than expected Canadian growth. The U.S. dollar reached its highest level (CDOL 1.2002) in over two years, before depreciating slightly during April.

PART IV: U.S. BALANCE OF PAYMENTS

U.S. external deficits continued to decline in 1991, the fourth consecutive year of improved performance. This performance was influenced by both cyclical developments and the effects of Desert Storm, but it also continued to reflect the underlying strength of U.S. competitiveness. This strength should again be reflected in further underlying improvement in 1992 external performance. (See Tables 3 and 4.)

Developments in 1991

Trade balance: The U.S. merchandise trade deficit declined in 1991 for the fourth consecutive year, to \$74 billion from \$108 billion in 1990. From the peak deficit in 1987 (\$160 billion), this represents a cumulative adjustment of \$86 billion -- reducing the imbalance by more than one-half over the course of 4 years.

Exports grew by \$27 billion in 1991, or 7 percent in value terms, reaching a total of \$417 billion. This percentage growth -- reflecting an 8 percent increase in export volume, coupled with a slight decline in export prices -- is approximately the same result as in 1990 but under significantly more adverse circumstances. Growth in real imports by other countries slowed in 1991, so that maintenance of real growth of exports implies an increase in the U.S. share of world trade.

As in previous years, capital goods were a major element of strength in U.S. export performance, accounting for approximately half (\$13 billion) of the increase in dollar value. Civilian aircraft exports slowed while computer equipment grew at the same pace as last year. In contrast, exports of oil-drilling equipment, industrial pumps, and hospital equipment all accelerated.

On a geographic basis, the pattern of U.S. exports shifted in response to strong economic growth in Latin American and East Asia and slowing growth in Japan and Western Europe. One third of the increase in exports went to Latin America, and this area replaced Europe as our fastest growing market. Exports of consumer goods, industrial supplies and materials, and even foods, feeds and beverages did nearly as well as capital goods in these markets.

Imports amounted to \$490 billion in 1991, down about \$8 billion from their 1990 level. The decline was more than accounted for by an \$11 billion decline in petroleum imports. The major factor was the 13-1/2 percent price decline in oil prices, although volume declined also. Non-oil imports, in contrast, were almost entirely unaffected by price rises, with the \$3 billion value increase reflecting volume growth. Classified by end-use category, the increase in overall imports reflected increases in capital goods and consumer non-durables categories.

Reflecting these import and export developments by product and area, the trade surplus vis-a-vis Europe increased substantially, to nearly \$15 billion compared with \$2 billion in 1990. The deficit vis-a-vis the Asian NIEs also improved, with the bulk of the improvement reflecting export gains as was the case for the balance with Western Europe. However, the deficit in trade with Japan widened in 1991, to \$44 billion from \$41 billion, as imports from Japan rose slightly while exports to Japan were flat.

Current account balance: The 1991 current account deficit, at \$9 billion, was under \$10 billion for the first time since 1982. This result overstates the underlying trend improvement in the current account, because it includes \$42 billion in support from allies in connection with Operation Desert Storm.

However, even abstracting from these non-recurring receipts, the current account deficit declined substantially in 1991, to the \$50 billion range, compared with \$92 billion in 1990. In addition to the \$34 billion reduction in the trade deficit, the surplus on services rose by \$10 billion, to \$36 billion. Investment income declined slightly, while transfers other than those associated with Desert Storm were roughly unchanged.

Capital account: There were substantial changes in the pattern of private capital flows between 1990 and 1991. Securities transactions showed the largest change, with very substantial increases in both U.S. purchases of foreign securities, and foreign purchases of U.S. securities. U.S. purchases of foreign securities rose by \$18 billion, primarily reflecting increases in stock purchases. Foreign purchases of U.S. securities, after falling to nearly zero in 1990, rebounded strongly to over \$52 billion. By contrast with the outflow, securities inflows were heavily weighted to purchases of bonds, while stocks went from net sales in 1990 to net purchases in 1991.

Foreign direct investment inflows in 1991 continued to decline from their extremely high levels of 1988-9, though the decline from 1990 to 1991 was only \$15 billion, compared with a \$35 billion decline between 1989 and 1990. U.S. direct investment abroad increased by about \$30 billion in 1991, roughly the same as in the previous two years. Net banking transactions showed a \$12 billion outflow -- probably in part reflecting retrenchment by Japanese banks -- compared with net inflows in the \$12-15 billion range for the previous two years.

### Prospects for 1992

Trade balance: Trade data for 1992 are available only for January and February, on a Census basis. The two-month average deficit, roughly \$4-1/2 billion per month, is nearly \$2 billion below the monthly average for the same period in 1990. Exports have been running over \$2 billion above year-earlier levels, while imports are running \$1 billion or so higher.

While monthly data are highly volatile, the pattern of recent monthly data is consistent with a continuation in 1992 of a gradual downward trend in the trade deficit, perhaps to the \$65 billion range from \$74 billion in 1991. However, prospects for further declines in the trade deficit are subject to particular uncertainty this year given the cyclical situation both in the United States and the other major industrial countries.

Both the strength of U.S. recovery, and the pace of activity in Western Europe and Japan, will be major determinants of how the trade balance develops over the year. If the U.S. recovery is gradual, as the Administration and most private forecasters project, import growth should remain relatively subdued for the remainder of the year. With only modest slackening of growth in Europe and Japan, export growth could be sustained at rates observed in recent quarters, particularly given the reemergence of Latin America as a strong-growing U.S. export market. However, any combination of a severe slowdown in Europe and Japan, or much stronger-than-expected U.S. recovery, could increase the likelihood of at least a temporary -- though modest -- rise in the deficit.

Current account balance: The current account deficit should continue to be lower than the trade deficit, since net services performance continues to exhibit a favorable trend. Receipts for a variety of services -- financial, medical and educational -- have grown much more rapidly than payments in recent years. The U.S. also remains attractive as a tourist destination. Investment income should also remain in surplus. U.S. direct investment abroad, much of it long established, has consistently been more profitable than foreign direct investment in the United States which is of a more recent vintage. This should remain so in 1992.

If services continue their trend improvement and investment income remains in surplus, the current account deficit (excluding Desert Storm receipts) should decline to below \$50 billion -- perhaps substantially lower -- in 1992.

#### The Turnaround in the U.S. Trade Deficit: A Longer Perspective

The trade deficit has undergone two dramatic swings in the last decade. Between 1980 and 1987, it went from a modest \$25 billion deficit to one of \$160 billion. Between 1987 and 1991, over 60 percent of this deterioration has been reversed. The average annual decline in the deficit (\$21.5 billion/year) has been almost identical to the average annual increase during the run-up (\$19.3 billion/year).

Two main factors can be viewed as major elements driving these swings -- relative growth in the United States and abroad, and the strength of the dollar, a major influence on U.S. competitiveness. For example, Europe's recovery in the early 1980s was delayed while that in the United States was strong. During the early to mid-1980s, the dollar appreciated sharply in exchange markets. In the second half of the 1980s, these trends were reversed. Furthermore,

secondary factors have affected external performance significantly, including oil price swings, the debt problems in Latin America, and the emergence of the Asian "Tigers" as large-scale suppliers of basic manufactures.

The sharp swings are reflected in export and import data. Exports (in value terms) grew only 1-1/2 percent annually during 1980-87, but by over 13-1/2 percent per year during 1987-91. The dramatic improvement in export growth characterized all major product groups and geographic areas except autos and parts and Canada where growth was still positive but less striking.

Growth in value of total imports showed a less dramatic shift, but there were important changes in particular products/areas. After double-digit annual increases in 1980-87, imports of autos and parts were virtually flat between 1987 and 1991. While this reflected the Japanese Voluntary Restraint Agreement initially, in more recent years the principal factor has been the effect of the establishment of new plants in the U.S. by Japanese firms.

More generally, growth in imports of manufactures (autos, capital and consumer goods) fell by over 2/3 (5 percent annually versus 15-1/2 percent) between the two periods in question. By the same token, growth in imports from Japan, Europe and the NIES grew by less than 2 percent annually in 1987-91, compared with nearly 14 percent between 1980-87.

The Relation Between U.S. Growth and the External Sector

The robust external performance since 1987 is yielding major benefits for the U.S. economy, particularly growth and jobs. The table below shows that in recent years, the U.S. export sector has been among the most dynamic in the U.S. economy and has made an enormous contribution to U.S. growth.

	<u>Net Exports &amp; U.S. Growth</u> (Billions of 1987 dollars)				
	<u>1987</u>	<u>1988</u>	<u>1989</u>	<u>1990</u>	<u>1991</u>
Export of Goods & Services	364.0	421.6	469.2	505.7	537.8
Imports of Goods & Services	507.1	525.7	544.9	557.0	558.7
Change in Net Exports from Previous Period	+ 12.1	+ 39.0	+ 28.3	+ 24.4	+ 30.4
GDP	4540.0	4718.6	4836.9	4884.9	4848.8
(Change in GDP from Prior Year)	(135.5)	(178.6)	(118.3)	(48.0)	(- 36.1)

Between 1987 and 1991, exports of goods and services grew by \$174 billion (in inflation-adjusted dollars). This increase in exports accounted for over 56 percent of U.S. GDP growth. Subtracting (slower) import growth over the same period, the change in net exports of goods and services accounted for 40 percent of overall U.S. growth. Furthermore, net exports have grown every year since 1987, contributing positively to overall U.S. growth.

In particular, the external sector significantly moderated the trough of the current economic slowdown. In the depths of the recession, the fourth quarter of 1990 and the first quarter of 1991, net exports of goods and services made a substantial positive contribution to U.S. economic activity. While the domestic economy (in constant dollars) shrank a total of \$126.5 billion in this period, real GDP as a whole fell only \$79.3 billion because of the \$47.2 billion boost provided by net exports.

There was, to be sure, substantial quarterly variation in real net exports in 1991. Nevertheless, the continued strength of real exports supported growth in 1991 as a whole, continuing the trend witnessed in past years. In 1991, the change in net exports added \$30.4 billion to GDP, despite the slowdown in major industrial country growth and a pick-up in U.S. imports in the middle of the year.

Recent economic estimates also highlight the critical role exports play in U.S. job creation. U.S. Commerce estimates point out that from 1986 to 1990 (the latest information available), U.S. merchandise exports contributed 25 percent, or 2.2 million jobs, to the growth in U.S. private industry jobs. Moreover, this estimate does not even include additional jobs created by growth in services exports. Furthermore, recent trends suggest that job growth in merchandise export production is faster than job growth in production for domestic consumption. The share of total private industry jobs supported by exports rose from 5.7 percent in 1986 to 7.5 percent in 1990.

Investment income data also highlight the benefits of the world economy to U.S. economic welfare. In recent years, income for U.S. citizens from investments in other countries has risen considerably faster than payments to foreigners. From 1987 to 1991, receipts from abroad from interest, dividends, and reinvested earnings rose by about \$10 billion (in constant dollars), while investment-related payments to foreigners increased by only about \$3 billion. Thus, net U.S. investment earnings have more than doubled from \$5 billion in 1987 to \$11 billion in 1991. As a net debtor, the United States is benefiting from low international interest rates, and, in particular, from lower interest rates in the United States than abroad.



PART V: ASIAN NEWLY INDUSTRIALIZED  
ECONOMIES (NIEs) AND CHINA

Overview

Under Section 3004 of the Omnibus Trade and Competitiveness Act of 1988, the Secretary of the Treasury is required to "...consider whether countries manipulate the rate of exchange between their currency and the United States dollar for purposes of preventing effective balance of payments adjustment or gaining unfair competitive advantage in international trade. If the Secretary considers that such manipulation is occurring with respect to countries that (1) have material global current account surpluses and (2) have significant bilateral trade surpluses with the United States, the Secretary of the Treasury shall take action to initiate negotiations...on an expedited basis...for the purpose of ensuring that such countries regularly and promptly adjust the rate of exchange between their currencies and the United States dollar."

It was concluded in the October 1988 report that Taiwan and Korea "manipulated" their exchange rates, within the meaning of the legislation. Pursuant to Section 3004, Treasury initiated bilateral negotiations with Taiwan and Korea for the purpose of ensuring that these two economies regularly and promptly adjust the rate of exchange between their currencies and the U.S. dollar to permit effective balance of payments adjustment and to eliminate unfair competitive advantage.

Treasury concluded that Taiwan in fall 1989 and Korea in spring 1990 were no longer directly "manipulating" their currencies within the meaning of the legislation. These findings were reaffirmed in fall 1990 and spring 1991. However, it was noted that Taiwan's external surpluses remained large and that, in both Taiwan and Korea, exchange rate policy would continue to have an important role to play in promoting economic adjustment.

In addition, the reports concluded that in Korea, liberalization of remaining exchange and capital controls was required to improve the functioning of the exchange markets and assure the full operation of market forces in exchange rate determination. In Taiwan, foreign exchange and capital controls were cited as impediments to the operation of market forces in exchange rate determination.

The fall 1991 report noted that Taiwan's external surpluses continued to remain large, and that controls on capital and flows and foreign exchange transactions, along with reported central bank intervention to dampen the rate of appreciation, hindered the operation of market forces in exchange rate determination. The report determined that Taiwan's exchange rate policies and foreign exchange and capital controls contributed to indirect "manipulation" of its currency.

It also cited Korea's trade and current account deficits, the decline in foreign exchange reserves, and the lack of government intervention in the foreign exchange market as evidence that Korea was not directly manipulating the exchange rate. However, Treasury remained concerned that pervasive exchange and capital controls continued to hinder market forces in exchange rate determination.

The Treasury Department has held a number of formal discussions with both Korea and Taiwan on their respective controls on exchange activities and capital movements, in addition to general banking and securities matters. Both Korea and Taiwan, in our judgment, must liberalize significantly the existing discriminatory restrictions placed on foreign institutions and generally let market forces play a greater role in their economies.

China's large external surpluses, including its growing bilateral trade surplus with the United States, substantial depreciation of the renminbi, and administrative controls over foreign exchange allocation and trade have prompted the Treasury Department to consider the applicability of Section 3004 to China. The previous three reports concluded that China's trade surplus with the United States was primarily due to causes other than exchange rate manipulation. However, it was noted that China's administrative controls over the external sector were of serious concern, and that the United States would pursue these issues with the Chinese authorities.

The remainder of this chapter provides a summary of economic and exchange rate developments in Korea, Taiwan, and China, as well as the Treasury Department's assessment of the applicability of Section 3004 to these economies. (See Table 5.)

## KOREA

The Korean won has further depreciated against the U.S. dollar in nominal terms since the fall 1991 report, although it has not depreciated in inflation-adjusted terms. The nominal depreciation reflects in part the continued adjustment in Korea's external accounts, where significant deficits emerged in 1991, as well as higher Korean inflation. However, the exchange rate continues to be influenced by pervasive foreign exchange and capital controls in Korea. These controls constrain the forces of supply and demand in the exchange market, distort trade and investment flows, and continue to position the authorities to manipulate the exchange rate through indirect means.

### Trade and Economic Developments

Korea's real GNP registered 8.4 percent growth in 1991, compared to 9.3 percent in 1990, and was in line with Korea's historic growth rates over the past three decades. Growth in 1991 was led by private consumption and fixed investment, with the construction and manufacturing sectors registering particularly strong performances. Inflation remained a concern, reaching 9.7 percent at end-1991. Unemployment was low at just over 2 percent of the labor force.

Korea's external accounts have undergone substantial adjustment since 1989. This adjustment -- which has moved the current account from a surplus of 2.5 percent of GNP in 1989 to a deficit of 3.2 percent of GNP in 1991 -- has resulted largely from an increase in imports caused by: the strong growth of the domestic economy; rising wage demands and other factors adversely affecting Korea's export competitiveness; and rising oil import prices and the longer term impact resulting from the Persian Gulf crisis.

A current account deficit of \$2.1 billion emerged in 1990 and grew to a record \$8.8 billion in 1991 (3.2 percent of GNP). This included a trade deficit of \$7.1 billion on a balance of payments basis (2.7 percent of GNP), up from a \$1.9 billion deficit in 1990. However, these deficits do not appear to be structural in nature; external deficits are expected to be eliminated by mid-decade.

According to U.S. customs data, the U.S. bilateral trade deficit with Korea in 1991 fell to \$1.5 billion, down 63 percent from 1990. This was based on a 7.6 percent increase in U.S. exports to Korea and an 8.1 percent decline in imports from Korea. In the first two months of 1992, U.S. Customs data recorded a trade surplus with Korea of \$126.3 million, compared to a surplus of \$13.5 million during the same period in 1991.

Reflecting the rise in the external deficits, Korea's gross and net debt figures rose in 1991. After declining steadily since 1985, Korea's gross external debt rose to \$39.3 billion at the end of 1991, a 24 percent increase from \$31.7 billion at the end of 1990. However, the 1991 figure was equal to only 14.5 percent of GNP, compared with 52 percent of GNP in 1985. Net external debt hit \$12.5 billion at the end of 1991, up from \$4.9 billion in 1990. Notably, the debt service ratio fell below 10 percent at the end of 1990 -- less than half the level of three years earlier -- and declined further to roughly 6.4 percent in 1991.

With the negative trends in the current account not fully offset by capital inflows, reserves fell from \$14.8 billion at the end of 1990 to \$13.7 billion by the end of 1991, representing 2.1 months of import coverage.

#### Exchange Market Developments

Under the "market average rate" (MAR) system of exchange determination, introduced on March 2, 1990, the won/dollar exchange rate at the beginning of each business day is equal to the weighted average of transactions in the inter-bank market on the preceding business day. Inter-bank and customer rates are allowed to float freely within specified margins, which were expanded in September 1991, and are to be further expanded this year. Exchange rates between the won and third currencies are set in accordance with dollar rates in international currency markets.

During the first twenty-four months of the MAR system (through April 10, 1992), the won depreciated 11.9 percent in nominal terms against the U.S. dollar. Foreign banks accounted for a large share of transactions in the inter-bank markets, generally between 40-60 percent of the total. The Bank of Korea (BOK) was not a direct participant in the market, and other government-owned banks accounted for only a small share of inter-bank activity.

The cumulative nominal depreciation of the won against the U.S. dollar since the first of these reports was issued in October 1988 now stands at 9.7 percent. Since the fall 1991 report, this nominal depreciation has accelerated; the Korean currency has fallen 3.3 percent against the dollar over the past six months. However, because of higher inflation in Korea than in the United States, the won has shown little change in real terms against the dollar over this period.

#### Foreign Exchange and Capital Controls

The Korean authorities maintain a comprehensive array of controls on foreign exchange and capital flows. These controls prevent market forces of supply and demand from playing a fully effective role in exchange rate determination, distort trade and investment flows, and provide the Korean authorities with tools for indirectly manipulating the exchange rate.

One of the most onerous controls is the requirement that foreign exchange banks obtain and review, prior to entering into most foreign exchange transactions, original documentation of an underlying commercial transaction. This "real demand" rule seriously hampers the development of Korea's foreign exchange market, reflects the government's continued controlling hand in the foreign exchange market and its fundamental lack of confidence in market forces, and is inappropriate for a country at Korea's stage of development.

Other exchange and capital controls severely restrict the use of short-term trade finance, such as stringent terms for deferred payments for imports. There are effective limitations on a variety of current account transactions such as travel and remittances. Direct portfolio investment in Korea was opened to foreigners for the first time in January 1992, but a number of restrictions -- including a 10 percent limit on total foreign investment in any Korean stock and a 3 percent limit on investment by individual foreigners -- has kept foreign participation in Korea's capital markets minimal.

Capital inflows in connection with foreign direct investment in Korea, as well as investment abroad or foreign borrowing by Korean residents, are also restricted. These and other controls hinder the ability of branches and subsidiaries of foreign companies located in Korea to obtain investment and working capital and even import finance.

The Korean government revised the Foreign Exchange Control Act (FECA) -- renamed the Foreign Exchange Management Act (FEMA) -- in the fall of 1991 to adopt a "negative list" approach to the regulation of foreign exchange transactions. The negative list approach establishes that all foreign exchange transactions are to be permitted in principle, with exceptional restrictions explicitly listed in the regulations.

While the move to a negative list is welcome in principle, it remains to be seen precisely how the FEMA and its associated regulations will be revised and how many restrictions will remain. The U.S. Treasury Department has conveyed to the Korean authorities the view that the negative list of restrictions should be short and that it should include significant relaxation or elimination of the underlying documentation requirement and of the restrictions on deferred payments for imports.

### Financial Policy Talks

Capital and exchange controls and other financial policy issues are the subject of the ongoing Financial Policy Talks between the Treasury Department and the Korean Ministry of Finance. Four formal rounds of these talks, and several informal rounds, have been held since February 1990, most recently in March 1992. The purpose of the talks is to provide a mechanism for addressing specific market access problems that U.S. banks and securities firms face in doing business in Korea, and for encouraging broader liberalization of Korea's financial, capital, and exchange markets. The importance of financial issues to the U.S.-Korean economic relationship was reflected by President Bush's and President Roh's agreement in January 1992 to resolve differences in this area.

Progress in the Financial Policy Talks over the last two years has been limited. The Ministry of Finance has taken some concrete measures to improve the treatment of foreign financial institutions in Korea. These steps include increases in the ceiling on issuance of certificates of deposit (CDs) by foreign banks, elimination of the ceiling on foreign banks' paid-in capital in Korea, and permission for foreign securities firms to establish branches in Korea.

However, significant denials of national treatment for foreign financial institutions in Korea remain. In particular, foreign banks continue to face severe difficulties in securing adequate access to local currency funding sources to service their traditional clients. The marginal increases in CD limits, while helpful, have been inadequate to address the local currency funding problem; the ceilings should be substantially expanded or eliminated altogether.

At the same time, discrimination against foreign banks in the interbank call money market persists, while another potential won funding source, the trust business, is hindered by the requirement that a high percentage of trust deposits be invested in low-interest government bonds. In the securities area, onerous criteria for branch establishment and a limited scope of permissible activities effectively limit the attractiveness of the Korean market for foreign securities firms.

At the March 1992 Financial Policy Talks, the Ministry of Finance presented an inter-agency workplan for developing a three-staged blueprint for comprehensive liberalization of the financial sector. Treasury welcomed the commitment to formulate such a blueprint as a positive step.

However, concerns remain about the approach of the initial workplan. In particular, the pace of implementation of later stages is determined by macroeconomic preconditions, including a balance or surplus in the current account, lower inflation, and a narrowing of domestic and international interest rate differentials.

Treasury has pointed out to the Korean authorities that financial sector liberalization will be required to reduce interest rates and domestic costs in order to attain the macroeconomic preconditions laid out in the plan. Most significant and troubling is that the plan delays addressing fundamental issues such as accelerating interest rate liberalization and deregulation of capital controls until later stages. Treasury has also encouraged the Korean authorities to incorporate into the blueprint a shift to indirect tools of monetary control. Action by the Korean authorities in modifying these policies will be necessary for the Korean economy to remain competitive internationally.

The Korean government has announced that it will consult with experts from the International Monetary Fund, the International Bank for Reconstruction and Development, and other research institutes as it formulates the final two stages of its financial sector liberalization blueprint. These institutions can provide detailed advice on formulating a tightly integrated blueprint with more timely implementation of the entire range of needed liberalization measures.

The first stage of the blueprint, which includes measures to be implemented in 1992 and 1993, was completed at the end of March. Announced actions include a marginal increase in CD issuance limits; expansion of CD and call market maturities; national treatment on stock investment for resident foreign financial institutions; some easing of the underlying documentation requirement; enhancing regulatory transparency; foreign membership in the Korean Federation of Banks and the Korea Financial Telecommunications Institute (facilitating membership in Korea's ATM network); permitting foreign exchange hedging by foreign securities firms; permitting over-the-counter bond trading by foreign financial institutions; and expansion of the daily foreign exchange fluctuation band. While these measures address to some extent individual difficulties U.S. financial institutions operating in Korea face, they do not comprise substantial liberalization of the market.

Through the Financial Policy Talks, Treasury will continue the dialogue with the Korean Ministry of Finance as Stages II and III of the blueprint for financial sector liberalization are formulated. These issues are also addressed in the financial services negotiations underway in the Uruguay Round of world trade talks.

#### Assessment

There continues to be no basis at this time for concluding that Korea is directly "manipulating" its exchange rate, within the meaning of the legislation. This assessment is based on the following factors: the emergence of significant trade and current account deficits in 1991, the decline in Korea's foreign reserves, the lack of evidence that the Bank of Korea is intervening directly in the exchange market, and the modest role of other government owned foreign exchange banks in the market.

Nonetheless, the exchange rate determination system in place in Korea, while an improvement over the previous regime, is far from a truly market-determined one. In particular, we remain seriously concerned that pervasive Korean exchange and capital controls significantly constrain supply and demand in the currency market. Liberalization of these controls -- especially the "real demand" rule for foreign exchange transactions -- is imperative to strengthen the role of market forces in exchange rate determination and in Korea's trade and investment flows.

Therefore, in the period ahead, the Treasury Department will continue to monitor developments in Korea's external accounts and the operation of the MAR exchange rate system. We will also continue to press for liberalization of Korea's financial, capital, and exchange markets, as well as to seek improved treatment for U.S. financial institutions in Korea.



## TAIWAN

The Treasury Department is increasingly concerned about the lack of appreciable adjustment in Taiwan's persistent external surpluses and the role of the exchange rate in the adjustment process. The exchange rate does not fully reflect forces of supply and demand, as market pressure for appreciation continues to be impeded by limitations on capital flows and on foreign exchange transactions, and by central bank intervention to dampen the rate of appreciation and limit speculation. This combination of practices contributes directly to Taiwan's efforts to generate the trade surpluses it views as necessary for reserve accumulation and impedes further adjustment of Taiwan's external imbalances.

### Trade and Economic Developments

After declining in 1990, Taiwan's overall external surpluses rose in 1991. According to its data, Taiwan's overall trade surplus for 1991 increased to \$13.3 billion, a 6.4 percent increase over 1990. Taiwan's global current account surplus increased by 11.6 percent in 1991 to \$12.0 billion, and remained at 6.7 percent of GNP.

Taiwan's bilateral trade balance with the United States declined at a modest pace in 1991. According to U.S. statistics, the U.S. trade deficit with Taiwan in 1991 was, at \$9.8 billion, 11.9 percent lower than in 1990. Imports from Taiwan increased by 1.8 percent while U.S. exports to Taiwan increased by 14.8 percent. In addition to slow growth in the U.S. economy, factors such as the relocation of Taiwan's labor-intensive export industries overseas, rising wages and production costs, and inflationary pressures continue to play an important role in reducing Taiwan's trade surplus with the United States.

The recent decrease in Taiwan's bilateral trade surplus with the United States is likely to slow or reverse as the United States recovers from recession. Taiwan's most recent data indicate that the bilateral trade surplus increased to \$2.6 billion in the first 3 months of 1992, compared to \$1.7 billion in the corresponding period in 1991.

Taiwan's official foreign exchange reserves, already the world's largest, increased significantly over the last year to reach \$83.2 billion at the end of February 1992 (sufficient to cover more than 17 months of imports), compared to \$76.4 billion (14 months of imports) at the time of the fall 1991 report. For purposes of comparison, the industrial countries hold non-gold reserves equivalent to 2-3 months of import cover.

Based on data for the first quarter of 1992, the current account surplus is likely to increase further in 1992. The economy should continue to grow rapidly; real GDP is expected to expand by 7 percent in 1992, following 7.2 percent growth in 1991. Inflation averaged 3.5 percent in 1991 and has increased to 4.4 percent in March 1992.

#### Exchange Rate Developments

The cumulative appreciation of the NT dollar since the last report is 4.2 percent. The currency appreciated 5.5 percent to reach a record high in mid-February. It has since depreciated by 1.3 percent through April 10, when the exchange rate stood at NT\$25.299/US\$1.

In the months since the last report, the Central Bank reportedly continued to intervene in the exchange market to moderate upward pressure on the NT dollar in order to control speculation and to maintain or improve the competitiveness of the export sector in response to political pressure. In addition, market pressures for appreciation have been resisted through the temporary imposition earlier this year of greater controls over inward remittances of foreign exchange by institutional investors, apparently because of pressure on the NT dollar.

Given the strength of Taiwan's economic fundamentals -- strong economic growth, the large and growing trade and current account surpluses, large and growing foreign exchange reserves, and a stable political environment -- market pressures for further appreciation of the NT dollar are likely to persist over the medium term.

#### Exchange Rate System

While Taiwan has instituted a number of measures over the past several years to liberalize the exchange rate system and reduce capital controls, as previous reports have noted, the exchange rate system does not allow the full effect of market forces to be reflected in the exchange rate. Though the rate for foreign exchange transactions is freely determined between buyers and sellers, intervention by the Central Bank to moderate the pace of appreciation and continued limitations on foreign exchange transactions and capital flows impede the full operation of market forces in exchange rate determination.

These practices are inappropriate and inconsistent for an economy with the stated objective of becoming a regional financial center. Several of the limitations are especially harmful to foreign banks and securities firms.

Taiwan continues to limit the amount of cash an individual can carry in and out of Taiwan (NT\$40,000 or about \$1,600). It also restricts annual non-trade-related capital inflows and outflows to \$3 million per individual or firm (capital flows for trade purposes are unlimited). The Central Bank should dismantle these limits as economic fundamentals are enhancing the stability of Taiwan's markets and reducing the opportunity for speculation.

Since the last report, Taiwan moved to the internationally accepted practice of using an accrual basis to calculate foreign exchange positions for banks, and reopened its forward foreign exchange market in a limited manner. Since this switch to the accrual method, overbought (long) and oversold (short) limits no longer have an effect on forward trading. However, significant restrictions remain that severely constrain forward trading, and thus limit the role of market forces in exchange rate determination and negatively affect a potentially major area of business for foreign banks.

For instance, forward transactions are permitted only for trade-related purposes. Similarly, foreign exchange liabilities ceilings, which vary from bank to bank, still affect forward trading, and also restrict the ability of foreign branches to offer foreign currency loans in Taiwan and to use swap funding for local currency lending. In place of these quantitative limits, prudential concerns in this area could be addressed through other means, such as through a risk-based capital requirement that would apply to the financial institution as a whole.

#### Financial Talks

The Treasury Department and Taiwan's authorities engage in financial policy talks under the auspices of the American Institute in Taiwan and the Coordinating Council on North American Affairs. These talks provide a forum for addressing specific market access problems encountered by U.S. banks and securities firms in Taiwan, and for encouraging Taiwan's authorities to undertake further liberalization of its financial and exchange markets, and of restrictions on capital flows. However, progress has come slowly.

We believe the authorities have been excessively cautious in their efforts to increase foreign participation in the financial sector. As a result, the international financial community is receiving mixed signals about Taiwan's commitment to develop as a regional financial center, with foreign participation.

In addition to the constraints imposed by Taiwan's controls on foreign exchange transactions and capital flows, U.S. financial services firms continue to face significant denials of national treatment. In many instances, there is outright discrimination against foreign banks and securities firms. For example, the number and location of additional foreign bank branches is still restricted. Foreign banks also cannot deal directly in short term-money instruments. Substantial restrictions are placed on foreign institutional investment in the stock market, while investments by foreign individuals are prohibited altogether. Foreign firms cannot manage private pension funds.

### Assessment

Taiwan's overall external surpluses increased in 1991, and substantial adjustment does not appear likely this year. While Taiwan's bilateral trade surplus with the U.S. declined somewhat in 1991, we do not expect this decline to be sustained over 1992 as growth resumes in the U.S. economy in coming months. Taiwan's foreign exchange reserves are also excessive, especially given the investment needs of the economy. These large and growing external surpluses indicate a need for substantial adjustment. Appreciation of the NT dollar must play a major role in this process.

In this context, official actions that are impeding market adjustment of the exchange rate are a matter of increasing concern. These actions may be motivated by the authorities' concern about a number of factors, including the declining share of total exports going to the U.S., a desire to maintain their large stock of foreign exchange reserves, and fear of speculation.

In addition to official action, limitations on foreign exchange transactions and capital flows remain far too restrictive and impede the full operation of market forces in exchange rate determination. Given the advanced state of economic development on Taiwan, and the stated desire of Taiwan's authorities to develop Taiwan as a regional financial center, such limitations should be completely lifted.

Under Section 3004 of the Omnibus Trade and Competitiveness Act of 1988, the Secretary of the Treasury must "consider whether countries manipulate the rate of exchange between their currency and the U.S. dollar for purposes of preventing effective balance of payments adjustments or gaining unfair advantage in international trade." It is Treasury's present judgment that Taiwan is manipulating its exchange rate within the meaning of the legislation. In the context of Taiwan's continued large bilateral and overall trade surpluses and foreign exchange reserves, recent official actions that directly interfere with the role of market forces in exchange rate determination, such as intervention in the foreign exchange market and imposition of controls on capital inflows, must be viewed as an effort by the authorities to inhibit effective balance of payments adjustment.

To promptly effect an appropriate adjustment in its external surpluses, the authorities should take steps that would allow the exchange rate to reflect fully market forces. Specifically, they should cease intervention in the exchange market, significantly reduce controls on capital inflows and outflows, while making a commitment to phase out the controls completely, and eliminate limits on foreign exchange activities in the banking sector.

Given our concerns, we will continue to monitor carefully the pace of adjustment in the overall and bilateral trade balance and the role of currency appreciation in that process. We will use our ongoing discussions to negotiate an end to practices that inhibit the operation of market forces in exchange rate determination, capital flows, and foreign exchange transactions. We will also continue to seek improved treatment for U.S. financial institutions.

## CHINA

The size and growth of China's external payments surpluses are a source of serious concern. These surpluses result in large part from pervasive administrative controls maintained by the Chinese authorities over the external sector of the economy, including a highly regulated system of foreign exchange allocation and direct controls on imports. At the same time, balance of payments adjustment in China has been hindered by continued devaluation of the administered exchange rate and controls on exchange rates in the nation's foreign exchange swap centers.

Since the last report, the Treasury Department has continued its consultations with the Chinese authorities on foreign exchange issues. The goals of these discussions have been to seek a more market-oriented system of foreign exchange allocation and exchange rate determination in China, and to promote adjustment in China's balance of payments.

### Trade and Economic Developments

China continued to record large external payments surpluses in 1991. The country's global trade surplus moderated slightly from \$9.2 billion in 1990 to \$8.9 billion last year. Merchandise imports are estimated to have increased over 22 percent, reflecting stronger domestic demand, while exports continued to record solid growth of nearly 18 percent.

China's current account surplus is estimated to have grown from \$12 billion in 1990 to \$12.2 billion last year (3.3 percent of GNP). Largely as a result, foreign exchange reserves climbed 47 percent from about \$30 billion at the end of 1990 to over \$44 billion, equivalent to about 10 months of imports, at the end of last year.

According to U.S. customs data, China's bilateral trade surplus with the United States also grew in 1991. The surplus rose from \$10.4 billion in 1990 to \$12.7 billion last year, an increase of 22 percent. China thereby surpassed Taiwan as the source of the United States' second largest bilateral deficit (after Japan).

The continued strength of China's exports lies behind the growing imbalance in bilateral trade. Chinese exports to the United States grew 25 percent in 1991, significantly faster than the growth of China's global exports. Footwear, furniture, and toys led the export drive to the United States, reflecting the continued transfer of labor-intensive production facilities from Hong Kong and Taiwan to the mainland. At the same time, U.S. exports to China rose a strong 31 percent in 1991 after falling in 1990. Much of the gain can be attributed to a solid recovery in U.S. exports of fertilizers, organic chemicals, and plastics following China's lifting of import restrictions on those products last year.

The bilateral trade imbalance has continued to grow in 1992. In the first two months of this year, the Chinese surplus reached \$2.6 billion, compared with \$1.7 billion in the same period of 1991. A nearly 40 percent surge in Chinese exports to the United States in the first two months accounts for the widening trade gap.

Domestically, China's real GNP is estimated to have grown 7 percent in 1991, following growth of 5.2 percent in 1990. Inflation, as measured by the consumer price index (which may understate inflation in urban areas), averaged only 2.1 percent in 1991 but is expected to reach 5 percent in 1992 as the domestic recovery continues.

In early 1992, the Chinese authorities announced a renewed commitment to broad economic reform, adjusting the policy line in place since late 1988. According to official pronouncements, further opening of the external sector of the economy is a central pillar of the new reform program. However, the actual implementation of the new program, as well as its application to the foreign exchange system in particular, remains to be seen.

#### Exchange Rate System

China officially has a dual exchange rate system. The administered rate, set daily by the central exchange authorities, generally applies to trade transactions under the state plan. There is also a second rate determined in foreign exchange adjustment ("swap") centers, where joint ventures and other foreign invested enterprises, domestic entities that are allowed to retain rights to their foreign exchange earnings, and certain individuals may buy and sell foreign exchange or foreign exchange quotas at rates established through a regulated auction system. Outside the official dual rate system, there is a sizeable, but diminishing, black market for foreign exchange.

The authorities use a variety of means to control the allocation of foreign exchange under the dual rate system. Foreign currency earned by a state enterprise must initially be surrendered to the Bank of China in exchange for local currency at the administered rate. After each sale, the government gives the enterprise a foreign exchange quota according to a retention ratio determined by the government. In 1991, it was announced that this ratio had been universally revised to 80 percent of foreign exchange earnings; however, it appears that retention ratios continue to vary greatly among regions, firms, and products, and many exporters appear to retain rights to considerably less than 80 percent of their foreign exchange earnings.

The authorities also restrict access to the nation's swap centers for prospective buyers and sellers of foreign exchange. Domestic firms are permitted to trade only retention quotas among themselves rather than foreign exchange itself. In addition, there are restrictions on the purposes for which foreign exchange obtained in the swap centers may be used. (According to rules published by the exchange authorities, foreign exchange may be purchased in the swap centers only for the importation of goods deemed by the state to be "necessary" for China's development.) Other restrictions include limitations on trading among different swap centers around the country and on non-trade-related foreign exchange transactions.

Together these controls on foreign exchange allocation serve to distort and restrict the underlying demand for and supply of foreign exchange in the swap centers. This in turn affects the swap rate itself, which therefore cannot be called a market-determined exchange rate. Moreover, the authorities are positioned to influence the swap rate more directly by intervening in the market or shutting down trading if fluctuations in the rate extend beyond set bands.

For a more detailed description of China's dual exchange rate system, see Treasury's fall 1991 exchange rate report.

#### Exchange Rate Developments

**Administered Rate:** On April 10, 1992, the official rate of the renminbi stood at 5.48 yuan to the U.S. dollar. This represents a nominal depreciation against the dollar of roughly 4 percent since the adoption of the "managed float" system in April 1991, nearly 5 percent since the last major devaluation in November 1990, and some 47 percent since the first of these reports was issued in October 1988 (when the rate stood at 3.72 yuan to the dollar). The recent exchange rate trends reflect the Chinese government's new policy of gradually devaluing the renminbi in small steps, rather than undertaking large, periodic devaluations.

From 1986 to 1989, the nominal devaluation of the renminbi against the dollar was not sufficient to offset the impact of rising prices in China. (Inflation averaged 7 percent in 1987, 19 percent in 1988, and 18 percent in 1989.) In real terms, therefore, the renminbi appreciated against the dollar over this period. However, as a result of the significant nominal devaluation since the end of 1989, as well as lower inflation in China over this period (2-5 percent), there has been renewed depreciation in real terms against the dollar over the past two to three years.



**Swap Rates:** At the end of 1991, the average exchange rate for the renminbi in China's principal swap centers was roughly 5.9 yuan to the dollar. This represented a nominal depreciation of 3.5 percent since the end of 1990. The depreciation trend has quickened in 1992: having broken through the 6 yuan level at the end of March for the first time in over two years, the Shanghai swap center rate rose (depreciated) to 6.2 yuan by mid-April.

As a result of these trends, the spread between the administered and swap rates has declined to about 10 percent, compared with 80 percent in 1989.

### Foreign Exchange and External Trade System

China's foreign exchange regime must be viewed within the framework of the country's broader economic policies. According to Chinese officials, the primary goal of balance of payments management is to secure enough foreign exchange to pay for priority imports and debt service, while ensuring a sufficient level of reserves. The authorities use a number of tools to accomplish this goal, including both the foreign exchange system and direct controls over imports and exports. These tools are often overlapping and redundant.

For example, an importer wishing to obtain foreign exchange for non-priority imports must obtain not only approval from the exchange authorities but also an import license from the trade ministry and explicit approval from the ministry responsible for enterprises producing domestic substitutes. The various approval processes do not necessarily operate consistently. Possession of an import license does not guarantee that an importer will be allocated foreign exchange, nor does approval of foreign exchange use automatically entitle the importer to a license.

In practice, it appears that the strict import licensing system is often the most significant obstacle to the importer's ability to obtain foreign exchange. Thus an effort to remove foreign exchange controls without a complementary effort to address direct trade restrictions is unlikely to result in a significant adjustment in China's trade flows. At this time, we see little evidence that the Chinese authorities are undertaking reforms which would address either of these sets of controls in a fundamental manner.

### Assessment

The size and growth of China's trade and current account surpluses, including its large bilateral trade surplus with the United States, are developments of major concern. Surpluses of this magnitude are destabilizing to the global economy and must be reduced. A principal cause of China's large surpluses is the network of pervasive administrative controls over external trade, which severely inhibit China's imports, including those from the United States.

In Treasury's view, the Chinese authorities also employ exchange rate policies to help attain their balance of payments objectives. The administered rate of the renminbi has been continuously devalued since 1989, first in large, periodic adjustments, more recently in small, gradual steps. According to the authorities, the devaluation policy is designed to eliminate costly export subsidies and to unify China's dual exchange rates. In this manner, the authorities are using exchange rate policy as a substitute for badly needed measures to eliminate domestic price distortions that undermine the competitiveness of Chinese producers and make export subsidies necessary. As for unification, this is a desirable goal in the long run; however, in the absence of fundamental liberalization of China's trade and domestic price systems, unification will not result in an exchange rate that reflects the underlying relative cost of China's products.

In addition to devaluing the administered rate, the Chinese authorities also influence the exchange rate in the nation's swap centers by controlling both the demand for and supply of foreign exchange in the centers. As a result, the exchange rate does not act in response to market forces as a principal determinant of China's trade flows. The fact that the average swap center rate has fluctuated relatively little over the past two years, notwithstanding the tremendous changes in China's trade patterns and build-up of foreign exchange reserves, is evidence that some form of control is being exerted by the authorities in the swap centers. This control in turn impedes effective balance of payments adjustment in China.

Under Section 3004 of the Omnibus Trade and Competitiveness Act of 1998, the Secretary of the Treasury must "consider whether countries manipulate the rate of exchange between their currency and the U.S. dollar for purposes of preventing effective balance of payments adjustments or gaining unfair competitive advantage in international trade." It is the present judgment of Treasury that China is manipulating its exchange rate within the meaning of the legislation. Given the size of China's external payments surpluses and the level of its foreign exchange reserves, continued devaluation of the administered exchange rate and control of swap center rates must be viewed as an effort by the authorities to frustrate effective balance of payments adjustment.

Until far-reaching reform of China's trade and domestic price regimes has been undertaken, further devaluation of the administered rate should be suspended. At the same time, the Chinese authorities should take a number of concrete measures to permit the exchange rate to reflect market forces more fully. These include steps to make foreign exchange allocation automatic for companies which either have import licenses or are authorized to import without licenses, thus removing a redundant layer of control.

The foreign exchange surrender system should be eliminated, allowing exporters to retain all of their foreign exchange earnings and to convert existing foreign exchange quotas into cash. China should also loosen controls on the nation's swap centers, expanding participation and allowable transactions, to develop the centers into true markets for foreign exchange. In addition, all existing laws and regulations pertaining to foreign exchange should be published, and any proposed changes to the regulations made available to the public in advance for review and comment by interested parties.

These and other issues have been the subject of discussions between the Treasury Department and the Chinese authorities launched in the summer of 1991. The Department intends to continue to use this forum to negotiate with China concerning its foreign exchange policies and to seek a more market-oriented system of exchange rate determination and foreign exchange allocation. At the same time, China's trade restrictions are the subject of a U.S. Government investigation initiated last year under Section 301 of the 1988 Trade Act.

PART VII: CONCLUSIONS

Signs of recovery are emerging in the United States, and there are a number of other positive developments among the major industrial economies. Inflation has come down and is continuing to drop significantly this year. Short-term interest rates have fallen in some G-7 countries. Consumer and business indebtedness problems are diminishing. And external imbalances are declining in most G-7 countries.

But, in most of the G-7 countries, current indications on growth are not encouraging. Europe is laboring under the burden of high real interest rates, reflecting the spillover effects of German economic policies throughout Europe. Japan's economy is slowing down as well.

Substandard growth in the major industrial countries generates substantial costs for the people in these countries, cutting income and raising unemployment to unacceptable levels. And healthy G-7 economies are also important to support the major economic reform efforts which are being pursued in the new states of the former Soviet Union, Eastern Europe, Latin America, and in parts of Africa and Asia.

In this context, through the G-7 policy coordination process, the major industrial countries have agreed on the need to intensify cooperative efforts to strengthen world growth. A concerted program of action on fiscal, monetary, and structural policies is required. All major industrial countries must contribute to the program, although the contribution of each will vary according to individual circumstances.

At their April 1992 meeting, the G-7 Ministers and Governors emphasized the need to reduce fiscal deficits in all countries with large budget deficits through credible medium-term consolidation strategies. This will reduce demands on private savings to facilitate needed capital spending.

Countries with large fiscal deficits, relatively high inflation, excessive wage developments, and tight monetary policy should work to reduce budget deficits in order to provide scope for reductions in interest rates. Other countries with large surpluses and declining growth should be mindful of the possibilities of strengthening domestic demand through appropriate measures.

In the United States, we will have to renew progress on deficit reduction, which was interrupted by the temporary surge in deficits created by the recession and deposit insurance outlays.

Concerning monetary policy, while lower interest rates are welcome, real interest rates remain high, hampering global investment and growth. Satisfactory progress on reducing inflation

and in fiscal consolidation would create a basis for easing the burden on monetary policy and lowering interest rates.

While the major industrial countries bear a special responsibility for promoting global growth and adjustment of external imbalances, major trading economies like Korea, Taiwan, and China also have an important role to play in this effort. This report provides an analysis of economic and exchange rate developments in Korea, Taiwan, and China, as well as the Treasury Department's assessments as to whether they are "manipulating" their exchange rates, within the meaning of Section 3004 of the Omnibus Trade and Competitiveness Act of 1988, to prevent effective balance of payments adjustment or gain unfair competitive advantage in international trade.

Korea's external accounts have adjusted dramatically since 1989, when the country had a current account surplus of 2.5 percent of GNP. In 1990, a current account deficit of \$2.1 billion emerged, which soared to \$8.8 billion in 1991 (larger than that of the United States). There has been an associated sharp decline in the U.S. trade deficit with Korea over the period, from \$6.3 billion in 1989 to \$1.5 billion in 1991. In the first two months of this year the U.S. recorded a small trade surplus with Korea. Factors contributing to this turnaround include import increases associated with strong domestic demand growth and higher oil prices, and rising wages and other factors adversely affecting Korea export competitiveness.

The Korean won has depreciated 9.7 percent against the dollar since the first report in this series (October 1988). Since the fall 1991 report, the won has depreciated more rapidly in nominal terms, but has shown little change in real terms against the dollar because of higher inflation in Korea than in the United States.

There continues to be no basis for concluding that Korea is "manipulating" its exchange rate within the meaning of the legislation, given: the emergence of significant trade and current account deficits in 1991; the decline in Korea's foreign reserves; the lack of evidence of direct intervention by the Bank of Korea in the exchange market; and the modest role of other government-owned foreign exchange banks in the market.

Nevertheless, pervasive Korean exchange and capital controls significantly constrain market forces in the currency market. Liberalization of these controls -- especially the "real demand" rule for foreign exchange transactions -- is imperative to achieve truly market-determined exchange rates and trade and investment flows. The Treasury Department will continue to press for liberalization of Korea's financial, capital, and exchange markets, and for improved treatment for U.S. financial institutions in Korea.

In Taiwan, substantial adjustment of external imbalances has yet to be achieved. Taiwan's overall current account surplus rose 11.6 percent in 1991 to \$12 billion, or 6.7 percent of GNP, and is likely to rise further in 1992. Foreign exchange reserves, already the world's largest, rose significantly last year and reached \$83.2 billion at end-February 1992 (sufficient to cover more than 17 months of imports). While Taiwan's bilateral trade surplus with the United States declined from \$11.1 billion in 1990 to \$9.8 billion in 1991, this shrinkage is expected to slow or reverse this year. U.S. data indicate that our trade deficit with Taiwan rose 6 percent in the first 2 months of 1992. From the time of the fall 1991 exchange rate report to its peak in mid-February, the New Taiwan (NT) dollar appreciated against the dollar by 5.5 percent. But in the period from mid-February to mid-April, the NT dollar reversed its upward trend and depreciated by 1.3 percent.

In the months since the last report, the Central Bank reportedly intervened in the exchange market to moderate upward pressure on the NT dollar to boost export competitiveness. Moreover, earlier this year, the authorities temporarily imposed greater controls over inward remittances of foreign exchange by foreign securities firms. These actions were taken in addition to existing restrictions on foreign exchange transactions and capital flows, which impede the full operation of market forces in exchange rate determination and which have been the subject of ongoing bilateral discussions.

In the context of Taiwan's continued large bilateral and overall trade surpluses and foreign exchange reserves, appreciation of the NT dollar must play a major role in achieving substantial external adjustment. Recent official actions that directly interfere with market forces in exchange rate determination must be viewed as an effort by the authorities to inhibit effective balance of payments adjustment. Therefore, within the meaning of Section 3004 of the Omnibus Trade and Competitiveness Act of 1988, it is Treasury's present judgment that Taiwan is manipulating its exchange rate.

To promptly effect adjustment in its external imbalances, Taiwan's authorities should: cease intervention in the exchange market; significantly reduce controls on capital flows, while making a commitment to phase out controls completely; and eliminate limits on foreign exchange activities in the banking sector. The Treasury Department will use ongoing bilateral discussions to negotiate for these reforms, as well as for improved treatment for U.S. financial institutions in Taiwan.

China's overall current account surplus remained very large in 1991, growing by \$200 million to \$12.2 billion (3.3 percent of GNP). By end-1991, China's foreign exchange reserves had risen by 47 percent to over \$44 billion (equal to 10 months of import cover). At the same time, China's bilateral trade surplus with the United

States increased sharply, from \$10.4 billion in 1990 to \$12.7 billion in 1991.

A principal cause of China's large external surpluses is China's network of pervasive administrative controls over external trade, which severely inhibit China's imports, including those from the United States. But it is Treasury's present judgment that Chinese authorities also employ exchange rate policy to help attain their balance of payments objectives. After several large, periodic adjustments of the administered exchange rate, the authorities have devalued the renminbi gradually by nearly 5 percent since the last major devaluation in 1990, and by 47 percent since October 1988 (the time of the first of these reports). The authorities are using administered exchange rate devaluation as a substitute for badly needed measures to eliminate domestic price distortions that undermine the competitiveness of Chinese producers.

In addition to devaluing the administered rate, the Chinese authorities are also influencing the exchange rate in the nation's swap centers, through controls on access to the centers and on the operation of the centers, so that the rate does not fully respond to market forces. The fact that the average swap center rate has fluctuated relatively little over the past two years, despite the sharp increase in China's surpluses and reserves, is, in Treasury's view, evidence of the extent of control exerted in the swap centers.

Given the size of China's external payments surpluses and reserves and based on the information now available to Treasury, Treasury views continued devaluation of the administered exchange rate and control of swap center rates, in conjunction with pervasive trade and exchange controls, as an effort by China to frustrate effective balance of payments adjustment. Therefore, within the meaning of Section 3004 of the Omnibus Trade and Competitiveness Act of 1988, Treasury now considers China to be manipulating its exchange rate.

To promptly effect adjustment of China's balance of payments, China should suspend further devaluation of the administered rate until far-reaching reform of China's trade, exchange, and domestic price regimes has been undertaken, and take a number of concrete measures (cited in the previous chapter) to permit exchange rates, including the swap center rate, to reflect market forces more fully.

The Treasury Department launched discussions with the Chinese authorities on these and other issues in the summer of 1991. The Department intends to use this forum to seek Chinese reforms which will bring about a market-oriented system of exchange rate determination and foreign exchange allocation in order to help permit effective balance of payments adjustment. At the same time, China's trade restrictions are the subject of a U.S. Government investigation initiated last year under Section 301 of the 1988 Trade Act.

APPENDIX

TABLES AND CHART

1. Economic Performance of Key Industrial Countries
2. Measurements of Dollar Movements Versus G-7 Currencies
3. Summary of U.S. Current Account
4. Summary of U.S. Capital Account
5. Asian NIEs and China: Trade and Currency Changes
6. Chart: Real Trade-Weighted Exchange Rate Indices for the Dollar, Yen, and DM



Table 1

ECONOMIC PERFORMANCE  
OF MAJOR INDUSTRIAL COUNTRIES

I. Real GNP/GDP (percent change; annual average)

	<u>1990</u>	<u>1991</u>	<u>1992</u>
United States	1.0	-0.7	1.6
Japan	5.2	4.5	2.2
Germany*	4.5	1.2	2.0
France	2.8	1.2	1.8
United Kingdom	1.0	-2.2	0.8
Italy	2.0	1.0	1.6
Canada	0.5	-1.5	2.3
Total G-7	2.5	0.8	1.7

II. Consumer Prices (percent change; annual average)

United States	5.4	4.2	3.1
Japan	3.1	3.3	2.2
Germany*	2.7	3.5	3.8
France	3.4	3.1	2.7
United Kingdom	9.5	5.9	3.7
Italy	6.5	6.4	5.0
Canada	4.8	5.6	1.7
Total G-7	4.8	4.2	3.1

III. Current Account (\$ billions and percent of GNP/GDP)

United States	-92 (1.7)	-9 (0.2)	-53 (0.9)
Japan	36 (1.2)	73 (2.1)	93 (2.6)
Germany*	48 (2.9)	-21 (1.2)	-14 (0.8)
France	-8 (0.7)	-4 (0.3)	-4 (0.4)
United Kingdom	-28 (2.6)	-8 (0.8)	-15 (1.4)
Italy	-14 (1.3)	-19 (1.7)	-20 (1.7)
Canada	-19 (3.3)	-21 (3.5)	-18 (2.9)

SOURCE: Data and forecasts for the U.S., other G-7 countries, and G-7 totals are from the IMF. The comparable Administration forecasts for 1992 U.S. growth and inflation are 1.5 percent and 3.0 percent respectively.

\* GNP and inflation data cover west Germany only; current account data cover all of Germany from 7/1/90.

Table 2

**Measurements of Dollar Movements  
 Vs. G-7 Currencies  
 Percent Appreciation (+) or Depreciation (-)  
 through 4/17/92**

Value of the Dollar in Terms of:	Since Dollar Peak 2/26/85	Since Plaza Accord 9/20/85	Since Louvre Accord 2/20/87	Since Previous Report 10/18/91
Japanese yen	-48.8%	-44.4%	-12.8%	3.0%
German mark	-52.0%	-41.6%	-8.7%	-1.5%
British pound	-40.4%	-21.8%	-12.5%	-1.5%
French franc	-46.8%	-35.3%	-7.3%	-2.2%
Italian lira	-42.2%	-34.8%	-3.4%	-0.9%
Canadian dollar	-15.8%	-14.1%	-11.0%	4.7%

Source: New York 9:00 a.m. exchange rates

Table 3

29-Apr-92 11:50:30

SUMMARY OF U.S. CURRENT ACCOUNT  
(MILLIONS OF DOLLARS, S.A.)

	Quarters												Annual	
	90:1	90:2	90:3	90:4	91:1	91:2	91:3	91:4	1989	1990	1991			
Total Exports	95244	97088	96638	100580	100549	103889	104018	108061	361451	389550	416517			
Agricultural	10740	10201	9819	9457	9819	9435	10047	10820	42185	40217	40121			
NonAgricultural	84504	86887	86819	91123	90730	94454	93971	97241	319266	349333	376396			
Total Imports	122781	121178	125398	128308	119087	119426	124867	126723	477368	497665	490103			
Petroleum	15806	12825	15456	18021	13215	12919	13101	12210	50920	62108	51445			
Non-Petroleum	106975	108353	109942	110287	105872	106507	111766	114513	426448	435557	438658			
TRADE BALANCE	-27537	-24090	-28760	-27728	-18538	-15537	-20849	-18662	-115917	-108115	-73586			
Partial Bal (Excl. Ag Exps & Petimps)	-22471	-21466	-23123	-19164	-15142	-12053	-17795	-17272	-107182	-86224	-62262			
Net Services	8901	6605	9205	13607	11992	11327	12112	9813	25102	38318	45244			
Invest. Income	3002	7	2802	6133	4902	2365	1863	234	2687	11944	9364			
Other Services	5899	6598	6403	7474	7090	8962	10249	9579	22415	26374	35880			
Total Transfers	-4031	-4693	-4326	-9280	16919	7108	-2881	-1417	-15492	-22330	19729			
Remits & Pensions	-1218	-1123	-1302	-1201	-1336	-1336	-1293	-1417	-4420	-4844	-5382			
Govt Grants	-2813	-3570	-3024	-8079	18255	8444	-1588	n.a.	-11072	-17486	25111			
NET INVISIBLES	4870	1912	4879	4327	28911	18435	9231	8396	9610	15908	64973			
CURRENT ACCOUNT	-22667	-22178	-23881	-23401	10373	2898	-11618	-10266	-106307	-92127	-8613			
Desert shield support incl. in in transfers	n.a.	n.a.	n.a.	4260	22674	11617	4604	3500	n.a.	4260	42395			

Treasury: OASIA  
Office of Balance  
of Payments Analysis

Table 4

SUMMARY OF U.S. CAPITAL ACCOUNT FLOWS  
(MILLIONS OF DOLLARS, S.A.)

	Quarters										Annual		
	90:1	90:2	90:3	90:4	91:1	91:2	91:3	91:4	91:1	1989	1990	1991	
US Reserve Assets (Incr(-)Decr(+))	-3177	371	1739	-1091	-353	1014	3877	1225	-25293	-2158	5763		
Other Govt Assets	-669	-800	-314	4759	1422	-493	3197	-553	1319	2976	3573		
Foreign Official Assets	-7022	5805	13341	20301	6631	-3105	3854	13205	8623	32425	20585		
Industrial	-6917	6393	13231	12840	-8411	-2923	28	2753	-238	25547	-8553		
OPEC	3094	193	-1699	575	988	-3162	-4352	2870	10738	2163	-3656		
Other	-3199	-781	1809	6886	14054	2980	8178	7582	-1877	4715	32794		
Banks, net:	13851	-8275	16984	-7252	1803	-27472	8799	5252	12127	15308	-11618		
Claims	57085	-17255	-9984	-24513	20598	1215	2325	-20710	-51255	5333	3428		
Liabilities	-43234	8980	26968	17261	-18795	-28687	6474	25962	63382	9975	-15046		
Securities, net	-8510	-4733	-3548	-8773	-715	15674	-3847	-5049	45963	-25564	6063		
Foreign Securities	-8756	-11160	-1014	-7546	-9430	-12833	-12533	-11419	-22575	-28476	-46215		
U.S. Treasury Securities	-1151	4287	24	-2029	3409	13434	-1468	1486	29618	1131	16861		
Other U.S. Securities	1397	2140	-2558	802	5306	15073	10154	4884	38920	1781	35417		
U.S. Direct Invest. abroad	-8985	-2858	-17792	-3802	-12052	-2008	-6659	-8779	-33387	-33437	-29498		
Reinvested Earnings	-5789	-4780	-5443	-6239	-7805	-5760	-5377	-4801	-22368	-22251	-23743		
Equity & Inter-co. Debt	-3196	1922	-12349	2437	-4247	3752	-1282	-3978	-11019	-11186	-5755		
For. Direct Invest. in U.S.	16269	9346	7060	4538	4336	7548	6100	4214	70551	37213	22198		
Reinvested Earnings	-3081	-912	-2760	-7256	-3958	-4508	-2166	-4169	-3844	-14009	-14801		
Equity & Inter-co. Debt	19350	10258	9820	11794	8294	12056	8266	8383	74395	51222	36999		
Other U.S.-Corp., net	2309	-1061	4936	-4349	-2924	-2836	451	n.a.	8035	1835	-5309		
Claims	1649	-1760	676	-2509	-1308	-2076	-1414	n.a.	2581	-1944	-4798		
Liabilities	660	699	4260	-1840	-1616	-760	1865	n.a.	5454	3779	-511		
NET CAPITAL FLOWS	4066	-2205	22406	4331	-1852	-11678	15772	9515	87938	28598	11757		
Statistical Disc.	18601	24383	1475	19072	-8522	8781	-4156	750	18369	63531	-3147		
TOTAL *	22667	22178	23881	23403	-10374	-2897	11616	10265	106307	92129	8610		