

China calls for new reserve currency

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Published: March 23 2009 12:16 | Last updated: March 24 2009 00:06

China's central bank on Monday proposed replacing the US dollar as the international reserve currency with a new global system controlled by the International Monetary Fund.

In an essay posted on the People's Bank of China's website, Zhou Xiaochuan, the central bank's governor, said the goal would be to create a reserve currency "that is disconnected from individual nations and is able to remain stable in the long run, thus removing the inherent deficiencies caused by using credit-based national currencies".

Analysts said the proposal was an indication of Beijing's fears that actions being taken to save the domestic US economy would have a negative impact on China.

"This is a clear sign that China, as the largest holder of US dollar financial assets, is concerned about the potential inflationary risk of the US Federal Reserve printing money," said Qu Hongbin, chief China economist for HSBC.

Although Mr Zhou did not mention the US dollar, the essay gave a pointed critique of the current dollar-dominated monetary system.

"The outbreak of the [current] crisis and its spillover to the entire world reflected the inherent vulnerabilities and systemic risks in the existing international monetary system," Mr Zhou wrote.

China has little choice but to hold the bulk of its \$2,000bn of foreign exchange reserves in US dollars, and this is unlikely to change in the near future.

To replace the current system, Mr Zhou suggested expanding the role of **special drawing rights**, which were introduced by the IMF in 1969 to support the Bretton Woods fixed exchange rate regime but became less relevant once that collapsed in the 1970s.

Today, the value of SDRs is based on a basket of four currencies – the US dollar, yen, euro and sterling – and they are used largely as a unit of account by the IMF and some other international organisations.

China's proposal would expand the basket of currencies forming the basis of SDR valuation to all major economies and set up a settlement system between SDRs and other currencies so they could be used in international trade and financial transactions.

Countries would entrust a portion of their SDR reserves to the IMF to manage collectively on their behalf and SDRs would gradually replace existing reserve currencies.

Mr Zhou said the proposal would require "extraordinary political vision and courage" and acknowledged a debt to John Maynard Keynes, who made a similar suggestion in the 1940s.

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