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Janet Yellen’s Role in US-China Economic Relations

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Janet Yellen, a distinguished American economist and policymaker, offers unique insights into China. She prioritized safeguarding American interests by advocating a “friend-shoring” strategy, diverging from Trump’s isolationism. Yellen’s commitment to boosting US investment and manufacturing was central to Bidenomics. Her tenure saw notable advancements, including the chip war. Dispelling the China currency manipulation myth, she refocused on domestic concerns like inflation and cautioned against complete China decoupling. Yellen promoted cooperation with China in various areas, from fentanyl control to climate change. Despite right-wing perceptions, she effectively protected US economic interests and improved US-China relations.

Keywords: US, China, economy, Yellen

Introduction

Janet Yellen stands out as a prominent figure in American politics and the economic arena. She is often seen flying economy class, displaying a consistently warm and approachable demeanor. Yellen’s humility, respectfulness, and formidable education set her apart from many of her peers in American politics.

Yellen, armed with a PhD from Yale, boasts an illustrious academic background, having excelled at renowned institutions such as Harvard, the London School of Economics (LSE), and UC Berkeley. This academic prowess is a defining aspect of her character, setting her apart in the world of American politics.

During her early career, Yellen coauthored several influential economics papers alongside her husband, Akerlof, himself a Nobel laureate in economics. Their collaborative efforts made significant contributions to the field of labor economics. Notably, they developed a business cycle model that incorporated wage inertia and placed a strong emphasis on fairness in the context of unemployment. Their work also introduced the fair wage-effort hypothesis, asserting that when a worker’s actual wage falls below their perceived fair wage, it can lead to reduced work effort and ultimately contribute to unemployment (Akerlof & Yellen, 1985; 1988; 1990). These seminal articles, published in prestigious journals, paved the way for Yellen’s subsequent role as an influential economist in government.

During her tenure at the Federal Reserve, Yellen orchestrated a gradual increase in interest rates, which was widely regarded as a success. This strategic move created room for the Fed to later cut interest rates during the COVID-19 pandemic, thereby stimulating the economy.

As the US Treasury Secretary, Yellen’s role expanded onto the global stage, where she wielded significant influence in shaping American economic relationships with other countries, with a particular focus on China. She recognized the paramount importance of economic cooperation with China, a stance that contrasted with

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others in American politics advocating for decoupling and containment. Yellen firmly believed that decoupling China was an unattainable goal and that fostering cooperation was not only feasible but also beneficial for the United States. Her diplomatic acumen and nuanced approach to international economic relations underscored her commitment to pursuing mutual interests and global stability.

Industrial Policies

The United States is actively working to shift its supply chains away from China, implementing a range of policies to facilitate this transition. China’s remarkable rise as a global economic powerhouse has been primarily driven by its manufacturing and export capabilities. Since its entry into the World Trade Organization (WTO) in 2001, China’s exports have grown exponentially, earning it the moniker of the “world factory”. China’s industrial output now contributes to a staggering 30% of the world’s total production, establishing it as a major global supplier of various products.

China’s evolution is noteworthy: From initially producing clothing and footwear, it has progressed to manufacturing electric cars and is poised to potentially surpass Japan as the world’s largest car exporter in 2024. This transformation underscores China’s concerted efforts to move up the value chain in its industries.

Janet Yellen has articulated the need to contain China by engaging in trade with like-minded nations and diversifying supply chains to reduce risks, while she also underscored the importance of cooperation with allies during the US-China business conference.

The Biden administration has pursued a “friend-shoring” strategy, strengthening relationships with like-minded nations such as Japan, South Korea, and even Vietnam. Despite Vietnam’s historical differences with the US as a communist country, it has emerged as a strategic partner. Both President Joe Biden and Chinese President Xi Jinping have visited Vietnam, highlighting its pivotal role as it navigates relations between great powers and benefits from their economic ties.

During the Trump administration, preceding the Biden era, the US initiated a trade war with China. While Janet Yellen did not advocate for a complete severance of ties with China, she chose to maintain the high tariffs imposed during Trump’s tenure. Her rationale was that this would diminish China’s influence in manufacturing and create more job opportunities in the United States.

China, in response, launched the “Made in China 2025” initiative to develop its high-tech industry. This was prompted, in part, by US sanctions against Chinese tech firms like Huawei. China invested heavily in its chip industry, attracting significant funding, and sometimes even encountering fraudulent schemes aiming to secure government support.

The ensuing “chip war” saw the US striving to prevent China from accessing advanced chips. Taiwan, regarded as a separate province by China, houses the primary chip manufacturers, with TSMC producing over 60% of the world’s advanced chips. The machines used in chip fabrication come from the Netherlands, notably ASML’s extreme ultraviolet (EUV) lithography machines, capable of producing 7 nm chips or smaller.

During Janet Yellen’s tenure as Treasury Secretary, the US made substantial investments to attract and accommodate foreign companies. It persuaded Taiwan to relocate chip fabs, such as TSMC, to Arizona, and Foxconn to Wisconsin, aiming to thwart China’s access to advanced chips. The US also obstructed China’s acquisition of EUV machines produced by ASML.

Despite these efforts, Huawei managed to develop its 7 nm chip for its latest phone, achieving a significant breakthrough. The US Secretary of Commerce, Gina Raimondo, subsequently emphasized that China should not acquire advanced chips and even issued a threat to Nvidia, an American firm producing artificial intelligence (AI) chips founded by Taiwanese individuals, warning against selling chips to China or risking government intervention in the company.

Currency Policies

China holds the distinction of being the world's second-largest economy by nominal GDP, but when measured by purchasing power parity (PPP), it surpasses all other nations to claim the title of the largest economy. This significant difference in rankings stems from the exchange rate between the US dollar (USD) and the Chinese Yuan (CNY).

China boasts a lower cost of living across various aspects of daily life, including college tuition, healthcare expenses, real estate, and consumer goods. The country's status as the "World Factory" further contributes to its reputation for producing affordable manufactured goods. As of December 2023, the exchange rate stands at approximately 1 USD to 7 CNY. However, when adjusted for purchasing power parity, the rate effectively shrinks to 1 USD to 4 CNY. This adjustment results in China's real GDP exceeding that of the United States by a substantial 20%, a fact supported by indicators like electricity generation, where China outpaces the US.

Interestingly, neither the US nor China readily acknowledges this economic reality. While the US has its own motivations, China's stance is more complex. China aims to maintain a low currency value to keep its exports competitively priced but avoids showcasing its economic strength openly.

Former President Trump accused China of currency manipulation, but this charge is not entirely accurate. China's economy relies heavily on importing resources, particularly energy resources, as it lacks domestic reserves. Manipulating its currency to keep it undervalued would result in higher costs for resource imports, which could potentially outweigh the benefits of cheaper exports.

Janet Yellen, drawing from her rigorous economic training, concluded that China was not manipulating its currency (Mohsin, 2021). Rather, the lower valuation of the yuan is a natural outcome of China's economic structure. Despite advancements in high technology, China's economy remains rooted in middle and low-end manufacturing. In contrast, the United States occupies the higher echelons of the value chain, justifying a stronger currency.

In response to inflation spurred by various factors, including monetary incentives related to the pandemic and the Ukraine War, Yellen urged the Federal Reserve to raise interest rates to cool the economy. This advice, stemming from her experience as the former Chairwoman of the Fed, was not heeded by the current Fed Chair, Jerome Powell, who has a background in law rather than economics.

By 2022, the US faced an inflation rate of 8%, which subsequently decreased to 3% in 2023 due to interest rate hikes. During this period, China experienced export growth owing to strong US consumption and the comparatively lower value of the yuan. However, China's economy, relative to the US, peaked at around 75% in 2021 but receded to approximately 60%. This decline was attributed to several factors, including US inflation, a rising US dollar value, China's delayed reopening, and a property crisis.

Yellen recognized that the low value of the Chinese yuan was primarily a result of market dynamics rather than government manipulation. As the US inflationary pressures eased and interest rates stabilized, the exchange rate between the USD and CNY experienced a slight decline, moving from 7.3 to 7 by the end of 2023.

Economic Cooperation

The Trump administration had pursued a policy of complete disengagement from China, characterized by a hostile and adversarial approach. In contrast, Janet Yellen advocated for a more amicable and constructive relationship with China. She firmly opposed the idea of decoupling from China, a stance that set her apart from many hawkish American politicians. Yellen believed that fostering a positive economic relationship between the United States and China would be mutually beneficial, as evidenced by various sources (Hussein, 2023; U.S. Department of the Treasury, 2023).

In 2023, Yellen made a visit to China and engaged in productive discussions with Chinese officials. This visit came in the wake of strained US-China relations, notably sparked by a dispute over a spy balloon. Several top US officials, including Secretary of State Anthony Blinken, Climate Ambassador John Kerry, and Secretary of Commerce Gina Raimondo, followed suit with their own visits to China. However, Janet Yellen's demeanor and humility left a lasting impression on the Chinese people. Her actions, such as bowing three times to Chinese Vice Premier He Lifeng, were appreciated by Chinese netizens for their sincerity and humility.

During the Trump era, the US had attempted to sever its ties not only with China but also with its allies. Yellen, on the other hand, advocated for increased dialogue with US allies and emphasized the importance of maintaining communication with China. She recognized that China was a pivotal player in the global economy, and any attempt to isolate it would have detrimental consequences.

Yellen also took into account the global economic landscape. Following the Ukraine War, Russia was excluded from the SWIFT payment system, limiting its ability to use the US dollar in international trade. Russia circumvented this restriction by turning to the Chinese yuan, achieving significant economic growth, and outperforming EU countries despite Western sanctions. Conversely, the credibility of the US dollar suffered as many countries initiated the process of de-dollarization. Yellen understood that excluding a major player like China from the world economy would ultimately harm the United States. China alone represents nearly 20% of the global economy, making decoupling an impractical and potentially disastrous choice.

Under Yellen's leadership, the US and China reached agreements on various issues. Notably, they cooperated to curb the production and export of illicit fentanyl, a deadly component of drugs responsible for thousands of deaths in the US each year. Chinese laboratories had been manufacturing fentanyl and its analogs, which were finding their way to the US through Mexico. In response to Yellen's demands, China restricted its export of fentanyl, contributing to a reduction in overdose deaths in the US.

Yellen also pressed China to limit carbon emissions, leading to ambitious commitments by Chinese President Xi Jinping to peak carbon emissions before 2030 and achieve carbon neutrality by 2060. China made substantial investments in climate initiatives, transitioning away from fossil fuels towards solar and wind energy. Chinese electric vehicle manufacturer BYD emerged as the second-largest EV brand globally, following Tesla.

In the realm of climate policy, the Biden administration reversed Trump-era policies by rejoining the Paris Agreement, and Yellen actively sought cooperation with China on climate matters, yielding positive results. Additionally, crucial military communication channels were reopened following Yellen's visit to Beijing, signaling a thaw in relations between the two superpowers.

Conclusion

Janet Yellen is indeed a highly regarded female economist known for her scholarly approach and rational economic thinking. Her perspective on China stands out in American politics, as she places a strong emphasis on dialogue and cooperation, which may be seen as more idealistic and rational than some of her peers. While her courteous attitude towards China has been misinterpreted by some as surrendering to China, a closer look reveals that her approach aligns with economic analysis and pragmatism.

Yellen's stance acknowledges the interconnectedness of the American and Chinese economies. She understands that decoupling from China could have adverse consequences for the American economy and undermine the United States' credibility on the global stage. The isolationist approach of severing ties with both China and US allies, as seen during the Trump era, has faced criticism for its potential negative impact.

Additionally, Yellen recognizes that the overvaluation of the US dollar and inflation have contributed to China's trade surplus, rather than solely attributing it to currency manipulation. Her prudent approach aims to safeguard national security, rebuild international alliances, and foster a constructive relationship with China.

While many of Yellen's policies are part of the broader strategy adopted by the Biden administration to address China's rise, her strategic wisdom and impeccable character as a scholarly economist are highly respected by the Chinese. Despite occasional differences, Yellen's approach is grounded in economic rationale and seeks a balanced and pragmatic way to engage with China, which has earned her recognition from both sides of the aisle.

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