

# Opportunity spend

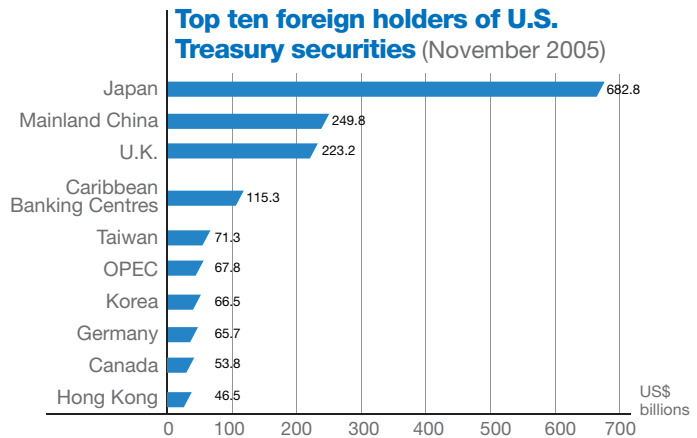
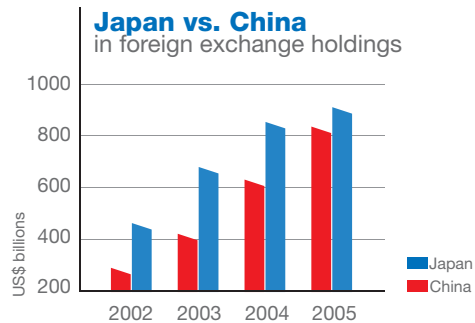
China is on track to overtake Japan as the world's biggest foreign exchange holder. Then what?

A big upsurge in China's foreign exchange holdings comes on the heels of a tripling of its current account surplus in 2005. Currently, China has nearly US\$819 billion in foreign reserves, second only to Japan at US\$847 billion.

The news has sparked concerns about the continuing imbalance in global trade and finance and the possibility that it will result in a painful market correction. Others worry that the news will encourage protectionist sentiments in the United States, despite the fact that Chinese purchases of U.S. Treasury securities help keep U.S. borrowing costs low.

The question for China is what to do with so much extra cash. There is little indication that China will lessen its dollar holdings, though foreign currency regulators have hinted at a shift in buying strategy that decreases the proportionate holdings of the dollar. This is in line with the trend of China foreign exchange holdings moving away from dollar denominated assets since 2000.

At the moment, a sudden depreciation of the dollar and its consequences are in no one's interest. However, the prospect of China using its clout to bolster debt markets denominated in other currencies is feasible.



While China is indeed set to become the world's number one in forex holdings in 2006, Japan's holdings of U.S. Treasury securities still dwarf those of China. Hong Kong is the tenth largest holder of U.S. Treasury securities.

