

China Cuts Holdings of U.S. Treasuries

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Foreign demand drops by record amount; Japan now holds most Treasuries

WASHINGTON - The government said Tuesday that foreign demand for U.S. Treasury securities fell by the largest amount on record in December with China reducing its holdings by \$34.2 billion.

The reductions in holdings, if they continue, could force the government to make higher interest payments at a time that it is running record federal deficits.

The Treasury Department reported that foreign holdings of U.S. Treasury securities fell by \$53 billion in December, surpassing the previous record of a \$44.5 billion drop in April 2009.

The big drop in China's holdings meant that it lost the top spot in terms of foreign ownership of U.S. Treasuries, dropping to second place behind Japan.

Japan increased its holdings of U.S. Treasuries, boosting them by \$11.5 billion to \$768.8 billion in December. That amount was higher than China's December total of \$755.4 billion, putting Japan back in the top spot in terms of foreign ownership of Treasury securities, a position it had lost in the fall of 2008 when China surpassed Japan.

The \$53 billion decline in holdings of Treasury securities came primarily from a drop in official government holdings, which fell by \$52.3 billion. The holdings of foreign private investors fell by \$700 million during the month of December.

For all of 2009, foreign holdings of U.S. Treasuries dipped by \$500 million. In 2008, foreigners had increased their holdings of U.S. Treasuries by \$456 billion as a global financial crisis triggered a flight to the safety of U.S. government debt.

That flight to safety had driven down the interest rates that the government was having to pay on its debt to record lows with rates on some short-term securities dipping into negative territory for brief periods.

The Obama administration on Feb. 1 released a new budget plan which projects that the deficit for this year will total a record \$1.56 trillion, surpassing last year's record of \$1.4 trillion deficit. The trillion-dollar-plus deficit have been caused by a deep recession, which has reduced government tax receipts, and the massive spending that has been undertaken to jump-start the economy and stabilize the financial system.

The administration has pledged to begin addressing the huge government deficits with Obama saying he will soon appoint a commission to recommend ways to trim future deficits.

Overall, the Treasury Department said that foreign net purchases of long-term securities totaled \$63.3 billion in December, down from \$126.4 billion in November. This category covers Treasury securities and private company bonds.

China's holdings are a result of the huge trade deficits the United States runs with China. The Chinese take the dollars Americans pay for Chinese products and invest them in Treasury securities and other dollar-denominated assets.

American manufacturers argue that China's huge dollar reserve reflect a strategy by the Chinese government to keep its currency artificially low against the dollar as a way to boost Chinese exports and dampen demand in China for American products.

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