China Is Getting Rid of Its $1 Trillion U.S. Debt Holdings Amid Washington's Escalatory Actions

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This year marks exactly 50 years since the establishment of ties between the United States and the People's Republic of China. US President Richard Nixon visited China in 1972 and initiated an unprecedented thaw in relations, the first ever between a Communist power and a leading capitalist one. It was a very unusual occurrence, especially as the (First) Cold War was reaching its zenith precisely at that time. Although Mao Zedong himself and Nixon paved the way for the establishment of this relationship, it was only after Deng Xiaoping took power that the modern Sino-American relationship grew and in many ways shaped the economic and geopolitical realities of our time.

At the time, China was still recovering from the last 200 years of decline which pushed probably the most powerful country in human history to the verge of collapse. This was followed by what can only be described as a semi-colonial status, culminating in the 1930s and 1940s, when Japan used China's weakness to occupy large swathes of Chinese land, often taking areas of utmost economic importance.

It was only with the establishment of the PRC in 1949 that this chaos ended, with extensive and crucial help coming from the USSR. By the 1980s, China became stable enough, but was still nowhere near its full potential. Deng Xiaoping focused almost entirely on the economy, realizing it was essential for China's full recovery and return to great power status.

China, the world's most populous country, offered the largest labor force on the planet, which (by American standards) was also cheap, making it the perfect choice for outsourcing entire sectors of the US economy, especially its industrial production. Although the Sino-American relationship went through a serious crisis in the 1990s, economic cooperation was booming and continued unabated into the 2000s. However, in recent years, this relationship has become burdened with geopolitical rivalry, particularly coming from the US, which has started meddling more aggressively in China's internal affairs, especially the issue of Taiwan.

Realizing the huge risks of any sort of cooperation with the belligerent thalassocracy in decline, particularly in light of sanctions against Russia, including the illegal freezing of Russia's forex reserves, Beijing is actively looking for alternatives. This is especially true in regards to China's holdings of US debt, which have been hovering around $1 trillion for over a decade. In order to avoid problems Russia faced after it was forced to intervene in Ukraine, China reduced the US Treasuries holdings from $1.003 trillion in April to $980.8 billion in May, the lowest it has been since 2010. With the US having to deal with high inflation, as well as strained bilateral ties with China over trade, technology and Russia, Beijing has decided to start dumping its share of US debt.

> "It's essentially a matter of China-US relations," said Tan Yaling, head of the Beijing-based China Forex Investment Research Institute, further adding: "The large holdings in the past were due to the good bilateral ties, but now China needs to avoid the risk of a possible conflict with the United States."

The reduction for the sixth straight month came at a time when Chinese academics and policy circles have held heated discussions over de-dollarisation amid the US strategic rivalry, including technological containment and the threat of decoupling, South China Morning Post reported.

Former central bank adviser Yu Yongding told a forum in Beijing in May that China should adjust its overseas asset portfolio, explicitly calling for cuts in holdings of US Treasuries, citing low returns and increasing worries over their safety, particularly in the context of illegal freezing of Russia's assets.

According to data from the State Administration of Foreign Exchange, China has been working on diversifying its foreign exchange assets for decades, with the USD share dropping from around 70% in 1995 to 58% in 2015. China's current US Treasuries holdings have been reduced by approximately 25% from the $1.32 trillion peak (November 2013) and 10.4% since Joe Biden took over office. US Treasuries now stand at 31.4% of China's $3.07 trillion forex reserves, the lowest share in the last nearly 15 years.

According to Tan, China is very likely to focus on buying gold, further implementing projects under its Belt and Road Initiative and resolving domestic issues amid the rising risks of a global recession. Between October 2018 and November 2019, the People's Bank of China (PBOC) increased its gold holdings by 105.75 metric tonnes, pushing the total to 1,948.

Short-term issues, including sharp rate increases and planned balance sheet downsizing by the US Federal Reserve, also weighed on the decision to cut holdings of US Treasuries, the analyst said. Japan, which took China's place as the largest holder of US debt also trimmed its holdings by nearly $6 billion at the end of May. It now stands at approximately $1.2 trillion, the lowest since January 2020. The UK, Switzerland and Belgium all reported net purchases in May, with London being the third-largest holder of US Treasuries at $634 billion at the end of June after adding US$21.3 billion.

As the world's largest production economy, China will continue to adjust monetary policies to domestic needs while taking into account external factors, as policymakers in Beijing are closely monitoring the US Federal Reserve's actions. Speaking at the G20 meeting over the weekend, Chinese central bank governor Yi Gang said the PBOC would provide more powerful support for the national economy.

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