The Combined Impact of Quantitative Easing and Interest Rate Hikes in the United States since COVID-19

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Abstract. The novel coronavirus epidemic has caused a huge impact on the US economy. In order to make the US economy recover as soon as possible, the US government has implemented a large number of expansionary economic policies. These policies have alleviated the negative impact of the US economy in the novel coronavirus epidemic to a certain extent, but it has spread to the world and laid the root of global inflation. In the implementation of expansionary economic policies for a period of time, high inflation also began to appear in the United States, to which the US government responded by violently raising interest rates. In 2022, the United States raised interest rates seven times, reaching 425 basis points in total. The US dollar appreciated sharply, reaps global benefits. In this research, the effects of these operations on China's inflation are described, and suggestions for getting rid of dollar hegemony and China's high-quality development are put forward.

Keywords: COVID-19, US interest rate hike, quantitative easing, inflation.

1. Introduction

Due to the impact of COVID-19, the US economy continues to be sluggish, residents' income has been hit, spending has declined sharply, the number of unemployed has risen, enterprises' expectations for the future market have declined significantly, and people are extremely worried about the uncertainty of the future, thus exacerbating the sluggish investment activities and causing a serious setback to the US economy [1]. In order to stimulate the economic development of the United States and ensure its sustainable prosperity, the United States adopted expansionary economic policies and quantitative easing policies. On March 27, 2020, the CARES Act was passed to issue a large amount of additional money to stimulate consumption, printing 2.3 trillion dollars, and the interest rate was even reduced to zero [2]. This measure alleviated the economiclosses of the United States to a certain extent. It also reduces the high unemployment rate that has soared in the United States since the pandemic, see Figure1. The loose monetary policy of the United States also has a huge impact on China's domestic inflation in many ways.

In every crisis, the US can always reap global benefits and diversify risks through quantitative easing or tightening fiscal policies on the basis of the US dollar hegemony. Thus, the suggestions for China to get rid of this dilemma and the methods to reduce the influence of dollar hegemony are conducive to China's long-term development in the future and the friendly relationship between various countries in the world.

This paper will firstly introduce the research background and significance, as well as the research ideas, innovations and shortcomings. Second, the literature on quantitative easing studied by predecessors is summarized and some general understanding is obtained to prepare for the follow-up analysis. The third step is to analyze the impact of the loose economic policy first adopted by the United States after the epidemic crisis on the domestic economy and China's inflation, as well as the transmission mechanism of China's domestic inflation from the two fields of economy and capital. The fourth point is the analysis of the contractionary economic policy adopted by the United States to deal with inflation, its mechanism of reharvesting global benefits, and its impact on China's economy, as well as the analysis of the reasons why China does not follow other countries in raising interest rates. The fifth point is proposed suggestions for China to reduce the negative impact of changes in US monetary policy at both the international and domestic levels. The sixth point looks

forward to China's future development prospects and puts forward suggestions for China's future high-quality development.

This paper combines the changes in the economic policies of the United States in the three years of the epidemic with China's inflation, analyzes its comprehensive impact on China's inflation, and shows the challenges faced by the RMB under the US dollar hegemony and the urgency to get rid of the US dollar hegemony from the perspective of inflation.

2. Literature Review

Expansionary economic policy was first proposed by John Maynard Keynes in the 1930s against the background of the Great Depression of the world economy. Different from the traditional Western economics which advocated the government living within its means, Keynesianism advocated expanding consumer demand to promote economic growth, such as increasing the government fiscal deficit and stimulating the economy to maintain economic prosperity. Later, in the process of gradual development, the cyclical budget balance theory was formed, which advocated that finance should play a countercyclical role [3]. With the development of The Times, this theory gradually fell behind and was gradually replaced by the functional finance idea. However, it does not simply pursue the ideal situation of government revenue and expenditure balance, reflecting the progress of economic theory with The Times. When many capitalist countries encountered economic crises, they adopted expansionary economic policies to solve the problems. For example, Japan's economy was depressed after the bubble burst in the early 1990s, and the Bank of Japan adopted the expansionary economic policies of cutting interest rates and issuing more money to deal with the crisis [3]. However, the expansionary economic policies adopted by other capitalist countries in the world normally have a huge impact on China's inflation. Taking the United States as an example, after the outbreak of the subprime mortgage crisis, the United States adopted expansionary economic policies to stimulate economic recovery. This caused China and other countries to bear the consequences of inflation and economic crises [4].

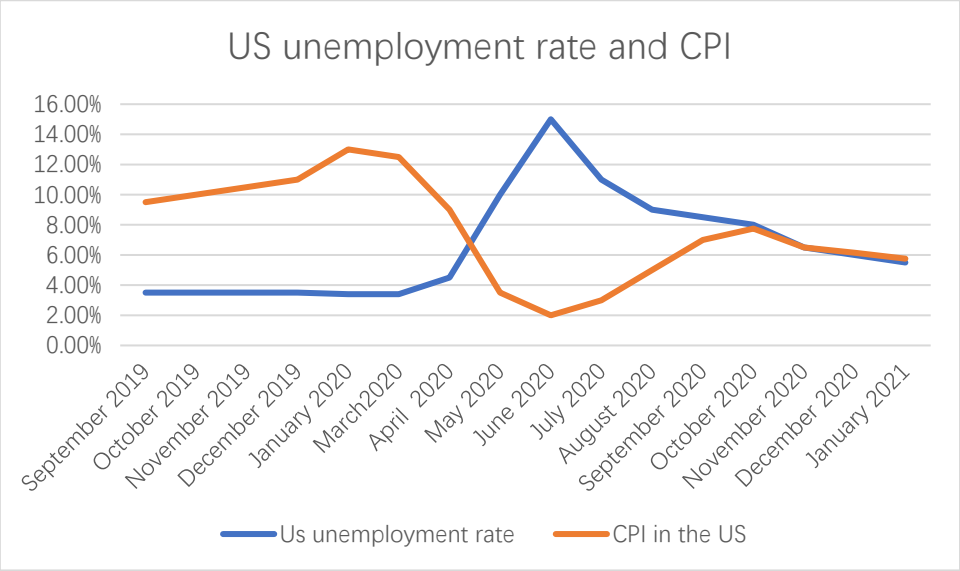


Fig. 1 US unemployment rate and CPI

3. The Impact of the Loose Economic Policy of the US on China

3.1. Transmission Mechanism in the Economic Field

First, the excessive printing of the US dollar leads to the depreciation of the US dollar. Then the loose monetary policy of the United States and the later complete liberalization of epidemic control in the United States stimulated retaliatory consumption in the United States, promoted the increase

of domestic consumer demand in the United States, increased the desire of the United States to import goods from China, and more domestic products flow to the United States, see Figure 2, resulting in the reduction of the quantity of Chinese products and the rise of prices, Trigger inflation [5].The large amount of Chinese goods imported by the United States will lead to the increase of China's foreign exchange reserve, but China implements the compulsory foreign exchange settlement and sale system, that is, the increase of foreign exchange is accompanied by the issuance of the same amount of RMB, which will increase the domestic money supply, further increase the commodity price, and promote the domestic inflation.

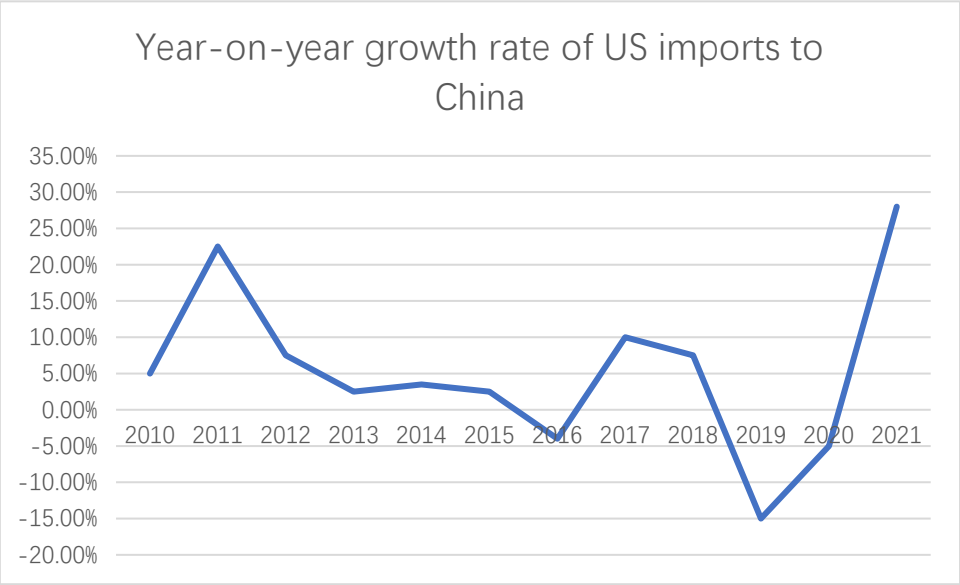


Fig. 2 Year-on-year growth rate of US imports to China

3.2. Transmission Mechanism of the Impact of Capital Sector on China's Inflation

In terms of capital flows, there are roughly three cases.

First, in terms of investment in the real economy, after the large-scale quantitative easing in the United States, some foreign enterprises think that they will face great competitive pressure at home and worry about the future economic situation during the economic turmoil, so they will consider going to countries with low labor price and low raw material cost, resulting in capital inflow. However, a large amount of capital flowing into China to build factories will greatly promote China's production, and bring about an increase in consumer demand, which will lead to inflation caused by overheated investment.

The second is the inflation caused by the wealth effect of capital speculation. After the United States issues a large amount of dollars, some short-term capital will flood into China's capital market to seize the opportunity of speculation to earn profits and raise the asset price in the capital market [6].

The third is related to China's compulsory foreign exchange settlement and sale system, because a large amount of capital inflow will lead to a rise in foreign exchange, and the central bank will trigger the same amount of RMB, which will increase the domestic money supply and lead to inflation.

4. Inflation in the US and Measures to Deal with it

However, the long-term expansionary economic policy of the United States has not only brought global inflation, but also brought inflation to the United States itself. In March 2021, the inflation rate of the United States broke through from 2% to 2.6%, rose to 4.2% in April, and reached 6.8% in November. This is the result of the continuous implementation of expansionary economic policies in the United States. In order to deal with the inflation crisis, the United States raised interest rates by a total of 425 basis points seven times in March [7], May, June, July, September, November and

December 2022, which is the largest interest rate hike in the United States in 40 years. Such a fierce interest rate hike will have many impacts on the United States, among which the high interest rate that has a positive impact on the United States will attract global capital to flow into the United States. The reason is that a considerable part of the funds of the investment industry around the world is borrowed from American banks. The increase of interest rate by the Federal Reserve will inevitably increase the repayment pressure of some enterprises and the desire to repay in advance. Increase in deposit interest rate will also allure many people to save money in the bank of the United States. Under the double influence, the United States will have more abundant funds, and when it enters the interest rate cut cycle in the future, there will be a large amount of funds to provide loans, which will further promote the development of the United States economy. In the long run, the United States will harvest the benefits of the world to boost its own economic development. In the short term, the decline in capital liquidity will make the dollar appreciate, even reaching the point of one-to-one exchange with the euro, promoting the development of the American import industry. Meanwhile, in the second half of 2022, through this round of interest rate hikes, the inflation rate of the United States will drop to 6.5 percent. But the most critical CPI, such as food and other necessities, is still high. Inflation continues to plague the United States, and its high interest rate also makes the debt problem of the United States more serious. Up to now, the debt of the United States has exceeded 30 trillion dollars [8], meaning that every one percent increase in interest rate, The United States is about to pay the debt of 300 billion yuan more, which has caused a great burden to the United States finance, and also increased the risk of the United States defaulting on its debt, making its credit decline, and laying the foundation for its possible credit crisis in the future.

5. The Impact of the US Interest Rate Hike on China

5.1. Inflation in China

The frequent interest rate hikes by the Federal Reserve also had a huge impact on China. First, the exchange rate of RMB and the US dollar fell below 7 in September 2022. The reason behind this phenomenon is that the interest rate hikes by the Federal Reserve led to the appreciation of the US dollar. Instead, three rounds of interest rate cuts were carried out, which led to the enhancement of the liquidity of the RMB, which in turn led to its own depreciation, while the US dollar appreciated during this period, so the exchange rate of the RMB against the US dollar naturally fell sharply [9]. At the same time, it has also had a great blow to China's import industry. According to the data released by the Russian Satellite News agency, China's import volume to the United States in 2022 fell by 1.1 percent year on year [10], and in December, the import volume was even less than a third of the export volume. Another result of RMB depreciation is a large increase in export goods, which leads to a decrease in the supply of domestic goods.

5.2. Analysis of Reasons for China Not Raising Interest Rates

This paper argues that the main reason why China does not raise interest rates to protect the exchange rate like other Western countries is that the impact of the epidemic on a country is roughly divided into three stages.

In the first stage, when the epidemic first broke out, almost all countries would adopt relatively closed policies, such as home isolation and work suspension, to prevent the spread of the virus. The second stage is that some countries will choose to open up for their own economic development. At this time, in order to better recover the economy, they will adopt expansionary economic policies, such as cutting interest rates and printing money. The third stage is to raise interest rates in order to curb the inflation caused by the expansionary economic policy in the second stage when the domestic economy improves. The United States and other countries are in the third stage, so choose to raise interest rates in order to curb inflation. However, due to the Chinese government's protection of the people, under the epidemic control for three years, people's demand has declined extremely, and social production has also suffered a great blow. If China chooses to raise interest rates again at this

time, it may lead to economic recession. This is not good for the whole of Chinese society. In addition, China's inflation rate of about 4% is not serious compared with other countries at this time, and it does not face the risk of extremely high inflation like the United States. Therefore, interest rate cuts and quantitative easing are undoubtedly the best choice at this time to stimulate people's demand and increase the desire of enterprises to borrow money to produce, so as to achieve the purpose of economic recovery.

Another factor analyzed in this paper for China's interest rate cut is that Chinese people prefer saving, see Figure 3. According to the data released by the People's Bank of China, the total amount of deposits of Chinese households increased by 7.45 trillion yuan in the first half of 2021 and 10.33 trillion yuan in the first half of 2022 [11]. According to the survey report of urban depositors in the second quarter of 2022 released by the People's Bank of China, the proportion of residents with the intention of "saving more" is as high as 58.3 percent [11]. It increased by 3.6 percent from the previous quarter, indicating that Chinese people's willingness to save has been rising almost every year, and this willingness has been further amplified by concerns about future risks due to the impact of the epidemic. This makes China different from other developed countries. Although China has a large amount of money, it is not easy to generate inflation, because the money saved is not liquid. Therefore, the amount of money in the market is still under control, so the inflation crisis in China itself is not serious, so there is no urgency to raise interest rates to curb inflation as in other Western countries, so the central bank chooses to cut interest rates.

The third reason is the real estate. The scale of China's real estate is huge, with an estimated total market value of 450 trillion yuan, which is involved in the development of various construction fields in China, such as building materials, environmental protection, graphic design, etc. [12]. According to the statistical survey of the People's Bank of China, housing accounts for nearly 70% of the total assets of urban households, which can be said to be an important industry related to the national economy and people's livelihood [11]. If China chooses to follow the footsteps of Western countries to raise interest rates, the pressure on the Chinese people from the 53.16 trillion yuan of mortgage loans according to the statistics of the People's Bank of China will further increase, and there may even be a large number of supply cuts and the risk of a large number of bad debts in banks. Moreover, under the impact of the epidemic, the people themselves are facing the pressure of not being able to repay the mortgage, so the interest rate hike at this time will undoubtedly make things worse. In 2022, there will be as much as 212.59 trillion yuan of loans in China. Choosing to raise interest rates after three years of control will undoubtedly greatly increase the domestic debt crisis and even cause a financial crisis [11]. The risks brought by raising interest rates are far less than the benefits, so the central bank chooses to cut interest rates.

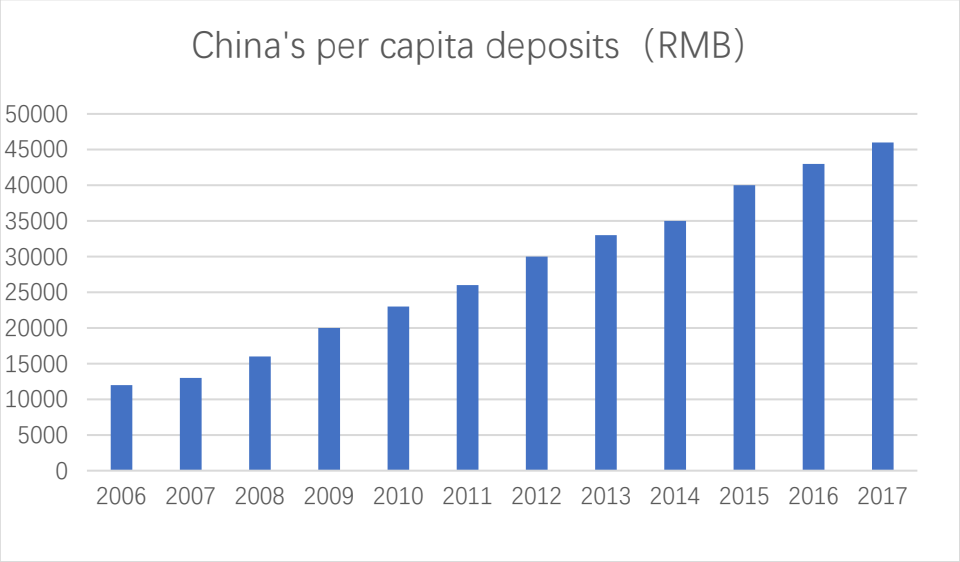


Fig. 3 China's per capita deposits (RMB)

6. Analysis and Suggestions on China's Reduction of the Impact of Changes in US Interest Rates

First of all, it is necessary to improve the status of the renminbi in the world and minimize the oppression caused by the dominance of the dollar and the economic impact on China. To do this, the first thing is to increase the frequency of RMB settlement through negotiations and interest exchanges with developing countries such as the Middle East, Southeast Asia, Africa and other developing countries in the process of international commodities and raw materials [13]. It is also suggested that the US debt can be forced to default by selling a large number of US bonds at a suitable time in the future, so as to achieve the purpose of reducing US dollar credit, and then suppress US dollar hegemony [14].

The second point is the basic guarantee of the above proposal, that is to enhance China's own comprehensive national strength, because the credit and value of the currency are based on the national guarantee, and only when China becomes strong and makes other countries believe that the use of the RMB will not be worthless due to national turmoil and can be exchanged for the products or services they want, which can essentially defeat the hegemony of the dollar.

It is also worth looking into Prospects for China's sustainable and efficient development in the future. When the economy is facing risks, the monetary policies implemented by a series of countries are no doubt the good medicine and necessary means to solve the crisis, but to prevent the arrival of the economic crisis is still the return to the essence of money. Money, as a general equivalent, does not have value itself, but the credit of the government and the products and services corresponding to money give value to money. The following are the suggestions for the future development of China's real economy:

First, increasing the restrictions on speculation, such as real estate speculation, which does not actually participate in production but only relies on poor information and luck to obtain wealth is essentially an invisible plunder of other people's wealth, which makes a group of people not participate in the creation of social value and reduces the efficiency of social production.

Second, reduce the scale of new real estate development. At present, the number of houses in China has been oversupplied, and blindly investing funds in real estate will only increase the number of unfinished buildings and waste of funds. Invest funds in agriculture, industry and other fields, effectively protect the interests of workers and farmers, and produce things of real value. Instead of repaying loans like real estate developers, forcing people to overdraw their future income and depress other consumption desires to repay mortgages, suppressed consumer demand will cause great harm to the social economy.

Third, lower the loan threshold for enterprises in the real economy, increase the preferential strength of the policy, effectively protect the interests of enterprises in the real economy, solve the loan difficulty and high interest rate situation, for some government engineering projects, the government should increase the investment of special funds, reduce the occurrence of arrears in project payments, and introduce preferential policies such as tax reduction and interest rate reduction[15]. Attract more people to enter the real economy industry to create real value for society.

7. Conclusion

From the beginning to the end of the epidemic, the United States has recovered its economy by changing monetary policy, increasing or reducing interest rates, and reducing the losses caused by the epidemic, but the risks brought by this series of operations have been dispersed to the world due to the hegemony of the dollar, harvesting the interests of other countries to strengthen itself, suppressing developing countries, blocking the upside of other countries, thereby further consolidating its hegemonic position. As the largest developing country, China has established foreign trade relations with a number of developed countries and actively promoted China's internationalization process, and a considerable part of the rapid development in the past few decades has been brought by providing cheap labor for developed countries such as the United States, which

makes China's economy more closely linked to the United States, so when the United States suffers from a crisis, it is usually implicated and has to share some risks for the United States, which seriously hinders China's progress, this also reflects the importance of dollarization In this paper, the reduction of money liquidity caused by savings is simply analyzed from the aspect of the reduction of the amount of money in circulation, but there is no research on whether the increase in savings will lead to an increase in borrowing and investment. It is suggested that future research could be conducted on these two aspects and reach more authoritative conclusions.

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