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On China Currency, Hot Topic in Debate, Truth Is Nuanced

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HONG KONG — Is China a currency manipulator?

Some of the more complicated exchanges during the presidential debate on Tuesday involved how to deal with China's efforts to increase its exports by keeping its currency at artificially low levels, an issue that has had considerable effects over the years on competitiveness, trade deficits and, some economists contend, American jobs.

Both candidates on Wednesday repeated the arguments they had voiced on the campaign trail. Mitt Romney criticized President Obama for not doing more to persuade China to stop intervening in currency markets. Mr. Obama said he was tougher toward Beijing than Mr. Romney would be if he were in the White House.

The two arguments obscure a more nuanced reality: adjusted for inflation, China's currency has strengthened considerably through much of Mr. Obama's tenure.

Some economists who used to be critical of China for undervaluing its currency, the renminbi, are now much less so. "Romney's vow to label China a currency manipulator is a position that is not supported by recent economic data," said Eswar S. Prasad, a Cornell professor who specializes in Chinese currency and trade policies.

But for all the improvement, those gains have recently stopped or started to erode. At the same time, Chinese exports to the United States are strengthening again, rising 5.5 percent in September from a year ago. That partly reflects increased demand as the American economy begins to show signs of recovery.

Mr. Romney was caustic in accusing China of unfair policies.

"One of the ways they don't play by the rules is artificially holding down the value of their currency," he said. "Because if they put their currency down low, that means their prices on their goods are low — and that makes them advantageous in the marketplace."

Mr. Romney promised that if elected he would immediately name China a “currency manipulator,” a designation that would mandate further negotiations with Beijing. It could lead to American retaliation if Congress passes legislation authorizing special tariffs for countries deemed to manipulate.

Mr. Romney was cautious, though, in threatening to actually impose tariffs on Chinese shipments to the United States, saying he would do so “if necessary.”

“On Day 1, I will label China a currency manipulator, which will allow me as president to be able to put in place, if necessary, tariffs where I believe that they are taking unfair advantage of our manufacturers,” he said.

Mr. Obama responded that the renminbi had strengthened 11 percent during his term of office. The value of one renminbi has actually risen 8.5 percent, to 15.9 cents, since he was sworn in.

But administration officials have tended to follow the practice of many economists in adjusting exchange rates based on the differences in inflation at the consumer level in two countries. Consumer prices have risen a little more than two percentage points more in China than in the United States since January 2009, according to official data, so the inflation-adjusted appreciation has totaled about 11 percent. Most of that took place in late 2010 and last year.

Economists say official data understates inflation in China much more than in the United States. The National Bureau of Statistics in Beijing has acknowledged that there are shortcomings in the way it calculates inflation and said it had begun to fix them. So the actual inflation-adjusted appreciation of the renminbi may have been even greater over the last several years.

That trend appears to be changing. As China’s economy has slowed over the last year, partly in response to its stronger currency, the pressure on prices has begun to ease. Exporters interviewed at the Canton Fair on Monday in Guangzhou, China, were unconcerned about inflation for the first time in years.

“Raw material prices are flat,” said Bob Wang, the sales manager at the Kralle Tools Company, a manufacturer in Wenzhou, in eastern China, that makes circular saw blades for lumber mills.

Through 2009 and the first half of 2010, China spent heavily to block the renminbi from rising against the dollar. China seemed to have the world’s healthiest economy during the global financial crisis that erupted in 2008. Its currency would have surged had it not intervened.

As it was, the central bank’s foreign exchange reserves swelled by $540 billion in just 18 months. The central bank paid for those huge purchases, mostly of dollars, partly by issuing more renminbi and partly by forcing the country's state-controlled commercial banks to hand over a fifth of their renminbi deposits at near-zero interest rates.

The central bank compensated the commercial banks by ordering all of them to pay very low interest rates — only half the rate of inflation — to their depositors.

Obama administration officials warned at the time that China was risking inflation by issuing so much more money. China's broadly measured money supply ended up growing 55 percent in 2009 and 2010, much more than that of the United States.

Inflation in consumer prices soon accelerated to reach 6.5 percent in July last year — nearly twice the American level, even before allowing for of China's tendency to understate inflation. Partly to brake inflation, by making imports cheaper, the Chinese authorities allowed the renminbi to start rising in the summer of 2010 after a two-year hiatus.

The combination of higher prices and a strengthening currency erased much of the undervaluation that institutions like the International Monetary Fund perceived early in the global financial crisis. The I.M.F. responded three months ago by reclassifying the renminbi to "moderately undervalued" from "substantially undervalued."

Chinese inflation has now largely disappeared because of strict controls on bank lending and a slump in the real estate market. Consumer prices are now rising at about the same pace in China as in the United States, while wholesale prices are dropping much faster in China than in the United States.

The daily fixing of the renminbi's value by the Chinese central bank is now almost exactly where it started the year, as the Chinese government has tolerated only small movements up and down this year. But there is little evidence the central bank is intervening on a large scale to suppress the value of the renminbi. It might even be acting to prevent it from going lower to avoid a political reaction in the United States.

Foreign reserves are essentially unchanged this year. The renminbi has been under downward pressure because Chinese businesses and households have been moving more money out of the country to diversify their investments and hedge against the possibility of political change at home; this has offset the tide of dollars still sweeping in from the persistent trade surpluses.

Chinese exporters have taken heart as the currency has stabilized and inflation has rapidly disappeared — although wages are still rising at a double-digit percentage pace. Vicky Leung, the sales director at the Xiangli Home Appliance Manufacturing Company, which makes electric fans in Shunde, in southeastern China, is one who is relieved.

“The dollar is good for us,” she said.