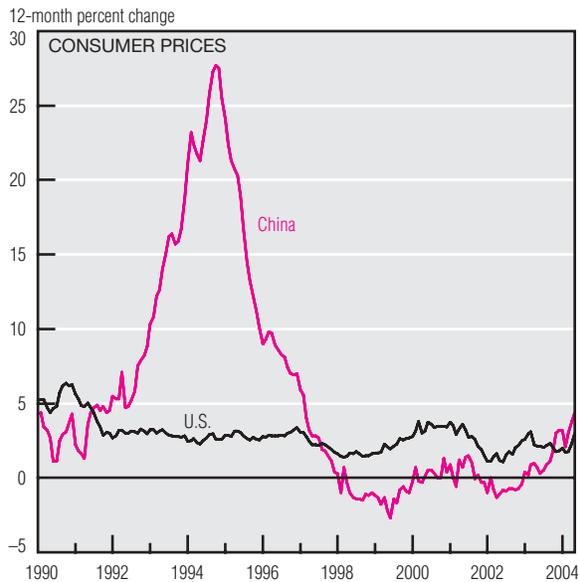
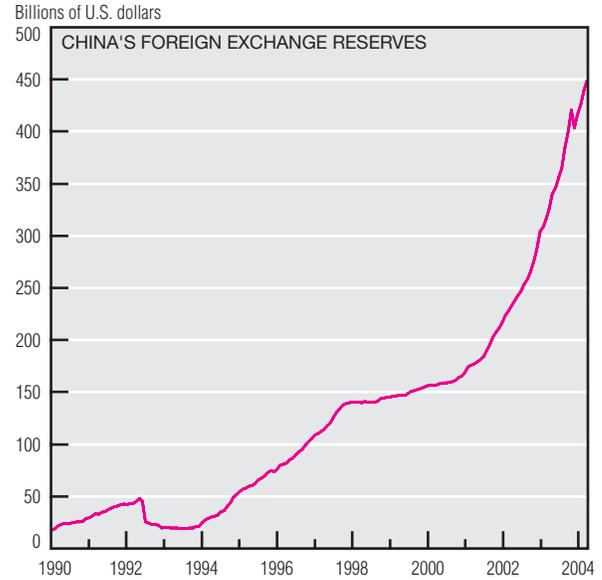
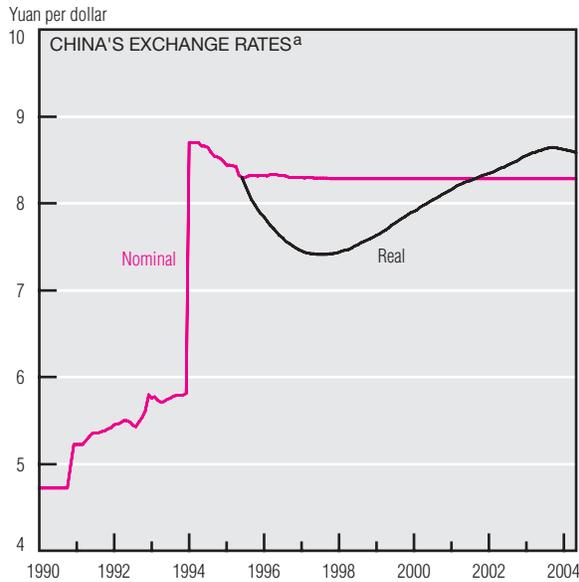


China's Renminbi: What's Real, What's Not



a. A rise indicates a depreciation of the renminbi. China's currency is the renminbi and its currency unit is the yuan. A renminbi consists of one yuan.

b. A rise indicates an appreciation of the renminbi.

SOURCES: U.S. Department of Labor, Bureau of Labor Statistics; and International Monetary Fund, *International Financial Statistics*.

In 1995, China pegged its currency, the renminbi, to the U.S. dollar at about 8.28 yuan per dollar. The often-made accusation that this peg undervalued the renminbi in relation to the dollar has some justification: China has acquired an enormous amount of dollar reserves under the peg. Had the renminbi floated against the dollar, it surely would have appreciated.

But the corollary claim that this peg has given China a huge artificial trade advantage is doubtful. Trade depends not merely on exchange rate movements—or lack thereof—but

also on relative inflation rates and many other things. Because China's inflation rate exceeded that of the U.S. until late 1997, the dollar actually depreciated relative to the renminbi on a real (that is, inflation-adjusted) basis during this time. Between late 1997 and late 2003, however, the relative inflation rates reversed, producing a real appreciation of the dollar relative to the renminbi. Recently, as China's inflation rate has again exceeded the U.S. inflation rate, the dollar has again depreciated slightly on a real basis against the renminbi.

The recent rise in Chinese inflation results in large part from China's accumulation of dollar reserves under the peg, because when the People's Bank of China acquires foreign reserves, it issues renminbi.

Overall, movements in China's real exchange rate since 1995 have not given that country a trade advantage relative to the U.S. or, for that matter, to China's other key trading partners. According to IMF calculations, since 1995 the renminbi has appreciated on balance on both a nominal and a real multilateral trade-weighted basis.