



China's Declining Current Account Surplus, Part II

Nicholas R. Lardy explains the policy implications for the United States of China's currency appreciation and lower current account surplus.

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Steve Weisman: This is Steve Weisman at the Peterson Institute for International Economics continuing my conversation with Nicholas Lardy, senior fellow at the Institute, moderate appreciation of the Chinese renminbi. Before I ask you what policy implications there over that appreciation, please summarize what you have observed.

Nicholas Lardy: China's currency, since they began appreciating in the middle of 2005, has appreciated by a little bit by more than 30 percent, and that has made a substantial contribution to the reduction in their external surplus, now down to 2.8 percent of GDP. China's surplus is now smaller, for example, than that of Germany.

Steve Weisman: This is a hot issue in Congress and it's actually becoming a little bit of an issue in the presidential campaign. Governor Romney charges that China is a currency manipulator. Are those arguments a little bit out-of-date because of these latest phenomena?

Nicholas Lardy: I think those arguments are substantially weaker than they were two or three years ago. First, as I've already mentioned, the best measure of Chinese currency—the Chinese surplus -- shows that it has come down dramatically over the last four years.

And secondly, the degree of intervention in the Foreign Exchange Market has also fallen quite significantly since the middle of 2011. We had very little intervention by the Central Bank after the middle of 2011. So now we're through to three quarters with relatively small amounts of intervention.

So, certainly, the main way a country manipulates its currency is through entering into the Foreign Exchange Market to either buy or sell currency to move the rate. China is doing that much, much less than they had been doing on average over the previous five or six years.

It's not that they've given it up completely, but I think it's fair to say that the rate today is much more determined by the market than it was a few years ago.

Steve Weisman: There are other indicators like in the holdings of foreign exchange reserves.

Nicholas Lardy: Yes, the reserves have not grown as rapidly. When the Central Bank is buying up foreign exchange, the reserves tend to grow. There was very little growth of China's foreign exchange reserves in the second half of last year.

We'll get the data for the first quarter of this year in another week or so and be able to make a more definitive judgment about whether or not that trend has continued for an additional quarter.

Steve Weisman: What would be your suggestion to the candidates and members of Congress in what they say and advocate about China now?

Nicholas Lardy: I think they should reflect a little bit better knowledge of the situation on the ground, recognizing that China's surplus has come down quite a bit, that their currency has appreciated quite a bit, that the degree of intervention in the market is substantially less than it was in the not-too-distant past.

I think that means the case for naming China as a manipulator, for example, is substantially weaker. I think what candidates should be doing and I think what President Obama should be doing, rather, is to recognize that the situation on the ground has changed for China, that they have moved their rate, that their surplus is down quite dramatically, and that we hope that that will continue to be the case. That would set a foundation for being critical, again, if the surplus should happen to rise in another year or two as a result of any one of the number of factors.

I think if you always criticize them and use the same language and the same volume, whether their surplus is going up or going down, the Chinese will start tuning out completely.

Steve Weisman: Thank you, Nick.

