REAL EQUILIBRIUM EXCHANGE RATE IN CHINA

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ABSTRACT

In this paper, we try to measure the size of a possible misalignment in the Chinese real exchange rate by two ways. On one hand, we address the issue of the “Balassa effect”, by which the real exchange rate of a catching-up country should appreciate. We compare China with other emerging countries, in order to assess the size of a “normal” “Balassa effect”. On the other hand, we follow the FEER (*Fundamental Equilibrium Exchange Rate*) approach. We use the NIGEM model for representing the foreign trade of China, the United States, the Euro area, South Korea and Japan. We calculate the real effective exchange rate that is consistent with sustainable current accounts. Both methods yield an undervaluation of the renminbi.

JEL Classification: JEL: F31, F33

Key Words: Renminbi, Balassa effect, BEER, FEER