The aim of the paper is to give some insights about the possible undervaluation of the Chinese currency. Firstly, we review the “usual suspects” for undervaluation by looking at different economic indicators. Secondly, we address the issue of the “Balassa effect”, by comparing China with other emerging countries. We try to measure the gap between the evolution of the real exchange rate in China and what would have resulted from a “normal” Balassa effect. We use two methods to assess this gap: cross-section estimations and panel cointegration. We evidence a lack of Balassa effect in China, consistent with the fact that the real exchange rate did not appreciate despite the rapid catching up. Thirdly, we use a FEER (Fundamental Equilibrium Exchange Rate) approach in order to get another idea of the existence and the size of the Renminbi’s misalignment. We use the NIGEM model for representing the foreign trade of China, the United States, Euro area, South Korea and Japan. We calculate the real effective exchange rate that is consistent with sustainable current accounts. Our results show that China’s real exchange rate was highly undervalued in 2002 and 2003 in effective terms and even more against the US dollar. Using the model with different assumptions, we analyse how the magnitude of currencies misalignments are modified with a lower deficit target for China. As expected, the Renminbi’s misalignment is less pronounced. Moreover, if we have taken into account the disguised unemployment, undervaluation would have been still weaker. Another interesting result is that the dollar’s misalignment is only weakly affected by the Renminbi’s misalignment. This suggests that a revaluation of the Renminbi would only have a small effect on the US external deficit.

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