

Macro Roundup Article

Headline: **Foreign Affairs**

Article Link: <https://www.foreignaffairs.com/united-states/china-still-rising>

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Publication	Foreign Affairs
Publication Date	April 05, 2024

Tweet: Nick Lardy argues that the stalling of China's economic convergence with the US is based on transitory inflation and interest-driven exchange rate factors and that China's nominal GDP measured in US dollars will surpass the US "in about a decade."

Summary: Take the widely held misconception that the Chinese economy's progress in converging with the size of the U.S. economy has stalled. It is true that from 2021 to 2023, China's GDP fell from 76% of U.S. GDP to 67%. Yet it is also true that by 2023, China's GDP was 20% bigger than it had been in 2019, the eve of the global pandemic, while the United States' was only 8% bigger. This apparent paradox can be explained by two factors. First, over the last few years, inflation has been lower in China than it has been in the United States. The growing gap between Chinese and U.S. interest rates reversed what had been a large inflow of foreign capital into China, ultimately depressing the value of the renminbi vis-à-vis the dollar by 10%. Converting a smaller nominal GDP to dollars at a weakened exchange rate results in a decline in the value of China's GDP when measured in dollars relative to U.S. GDP. But these two factors are likely to be transitory. China's nominal GDP measured in U.S. dollars will almost certainly resume converging toward that of the United States this year and is likely to surpass it in about a decade.

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Primary Topic: China

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