

## Report on “Is the Chinese currency substantially misaligned to warrant further appreciation?” by Duo Qin and Xinhua He

### General Comments

This is a key topic in international finance with profound policy implications. There have been many attempts to answer the question but large disagreements remain. This paper “attempts to produce more credible estimates of RER misalignments of the RMB by improving on the use of both modelling methods and data.” Unfortunately, it appears to provide just another set of estimates to throw into the pot rather than resolving the question.

### Specific Issues

1. The method adopted in this study is not ideally suited to the question of fair value of the Chinese currency. The approach is based on statistical equilibrium and supposes that, on average, the exchange rate in question is at fair value (in a single exchange rate context). However, the Chinese currency has been managed for the entire sample period and has not been allowed to fully adjust to market forces. The authors need to do more to convince the reader that a statistical approach is valid in this context.
2. The authors use a very restricted set of fundamentals (productivity differentials and relative net foreign assets) to assess fair value. While I appreciate there are data limitations, I would like to see some justification of this choice of fundamentals since the theoretical work this research is based upon (and much of the subsequent empirical work) uses a much richer set.
3. Related to this, the decision to drop interest rates from the model “because of the significant domestic control on interest rates and capital mobility in China” raises more issues than it answers. What is the effect on the estimates of including interest rates? Is there not a better way of including the effect of interest rates in the model than simply dropping them? If interest rates are affected by capital controls is it reasonable to assume that exchange rates are not?
4. There are no standard errors reported for the estimates of the fair value of the exchange rate. Instead, readers are confronted by a range of point estimates and an averaging of those estimates. Given the wide range spanned by the fair values estimated using different techniques, this paper faces the same problem as the literature – a range of point estimates that suggest anything from 20% undervaluation to 15% overvaluation.