The Washington Post

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Trump just took credit for something China did in 2014

By Ana Swanson May 12

President Trump's interview with the Economist contains a few strange claims. But while his “prime the pump” comment became an Internet sensation after the interview published Thursday, he made another less-noticed boast that was equally absurd — and more consequential.

Trump appeared to claim credit for China reversing its long-held practice of intentionally holding down the value of its currency to make its exports relatively cheap and boost business abroad.

“You know, since I’ve been talking about currency manipulation with respect to them and other countries, they stopped,” Trump said about the Chinese.

Treasury Secretary Steven Mnuchin, who spent decades working on Wall Street and in hedge funds, backed up Trump's specious claim. “Right, as soon as the president got elected they went the other way,” said Mnuchin.

The claim is patently untrue. For roughly a decade and a half leading up to 2014, China did depreciate its currency, to the detriment of U.S. businesses. But data shows that China abandoned the practice long before Trump came into office.

“The timing of Mr. Trump’s claims to have affected the dynamics of the Chinese currency simply do not stand up to reality,” said Eswar Prasad, a professor of international trade at Cornell University and the author of a book about China’s currency.

“The reality is that the Chinese currency started falling in value against the U.S. dollar almost a year before Mr. Trump had even declared that he was going to run for the Republican nomination for president,” Prasad said. “The Chinese would have had to have been extraordinarily farsighted to foresee Mr. Trump’s rise to power in order for him to influence China's currency policy.”

Just as for a given product, the value of a currency is determined by the market forces of supply and demand. Lots of factors can influence the demand for currency and thus change its price, including the level of interest rates and the pace at which a country’s economy is growing.

In countries that have barriers to the free flow of international investment, like China, the government can also intervene to influence a currency's value. In China, the government has a history of selling huge amounts of its own currency and buying U.S. dollars. The practice lowers the value of the Chinese currency, the renminbi, which helps to boost Chinese exports. It also leads the Chinese government to accumulate a massive amount of what are called foreign exchange reserves.

By tracking the level of foreign exchanges reserves, you can essentially see how much China was intervening in its currency market, and in which direction. And this metric tells a very different story than President Trump and Secretary Mnuchin did this week.

China accumulated about $3.8 trillion dollars of foreign reserves between early 2000 and the middle of 2014, as it held down the value of its currency to boost its exports. But by mid-2014, the country began to reverse the practice. At that point, the country's foreign exchange reserves start to decline, indicating that the country was no longer depreciating the currency, but actually working to prevent it from falling in value.

Throughout the campaign, Trump criticized China for intentionally holding down the value of its currency, a practice that hurts U.S. exporters. But in recent months, Trump changed his stance. In a Treasury Department report in April, the administration declined to name China a currency manipulator. Economists say Trump's decision was the correct one — but his description of China's actions is not.

China's shift in currency policy did have something to do with the United States, Prasad says — namely, the U.S. Federal Reserve's indication that it would begin raising interest rates. Because higher interest rates give investors better returns on their money in the United States compared to elsewhere, the prospect caused investors to pull their money out of emerging markets like China and invest in the United States — a process that put downward pressure on the renminbi and upward pressure on the dollar.

But while the U.S. central bank played a role, the shift in China's currency was largely due to internal developments. By mid-2014, the Chinese leadership was concerned that too much capital was flowing out of China. Chinese investors had begun to invest abroad, both to diversify their holdings and to hedge against the potential of a slowdown in their economy.

Additionally, the Chinese government began an intense crackdown on corruption among government officials, a practice that encouraged many people to send their savings abroad for protection. In early 2015, a stock market meltdown only intensified the pressures for people to get their assets to a perceived safe haven like the United States — leading to a surge in investment in U.S. companies and property.

The huge outflows of money naturally pushed down the value of the Chinese currency, as Chinese who wanted to send their money abroad sold renminbi and bought foreign currency. As the value of the renminbi dropped, the effect became a self-reinforcing process — investors who expected the value of the Chinese currency they were holding to drop decided to sell it before it lost any more value.

So the Chinese government began intervening to stop this vicious cycle, selling its U.S. dollar holdings and buying its own currency to prop up its value.

"It did have something to do with U.S. economics, because the notion of the Fed tightening rates was something that pulled capital out of emerging markets," said Prasad. "But the principal factors were all related to China's own economic situation."

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