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China Isn't Overtaking America

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NEW YORK — A report last month that China's economy will soon become the world's largest has sparked worries. Normally calm observers are taking the news as a sign that China is overtaking America as an economic power.

But much as counting warships or troops often provides a misleading measure of military might, tallying up gross domestic product — the figure behind the latest headlines — yields a warped picture of China's economic rise.

By most meaningful yardsticks, China is still less economically powerful than the United States. The problem with the new numbers starts with how they compare economies' sizes. The World Bank tables that show China passing the United States compare the two countries using "purchasing power parity," which measures national incomes in terms of what they can buy at home.

Because domestic spending is dominated by items such as food and housing that aren't traded internationally, and because most goods and services are cheaper in China than in the United States, this comparison boosts China's apparent economic strength.

Yet compared using market exchange rates, which measure incomes in terms of what they can buy on international markets (where every country pays the same price), the United States' economy remains nearly twice as big as China's. Indeed it is this latter measure that matters most when comparing economic power.

After all, one would never compare two countries' military strengths on the basis of how well each could suppress a domestic rebellion rather than fight a foreign war, and one should not compare countries' economic power on the basis of what a worker in each country can buy at home.

When American and Chinese companies bid against each other to acquire resources or companies abroad, what matters is their wealth as measured by the global market. Oil suppliers, for example, don't care if the \$100 they get for a barrel sold to China can buy more rice in a Beijing market than at a shop in New York — they care about what their revenues are worth in the world market.

Similarly, the attractiveness of the Chinese and American markets to foreign firms depends on the profits to be made in international terms, not as measured by purchasing power.

The alarmism about China surpassing America also ignores the critical role of political and institutional strength and flexibility. One wouldn't compare countries' arsenals while ignoring their different states of disrepair — yet Chinese G.D.P. numbers ignore severe pollution problems that are driving successful Chinese abroad. Nor would one compare numbers of aircraft or troops without asking about the training, doctrine and organization necessary to mobilize them effectively in combat. China faces real challenges translating its economic resources into international influence.

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