"Can China Sustain its Growth? China's Economic Challenges in the Next Ten Years"
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SEEKING NEW DRIVERS OF ECONOMIC GROWTH IN CHINA
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The Chinese Economy:
• Challenges in 2012
• Futures Trends
• Major Reforms Needed

I. Challenges:
Global Economic Slowdown
• Chinese economic growth rate in exports and imports has been declining since 2008.
  Although there was an increase in growth during 2010 when the economy recovered from the financial crisis, since 2011 it has been declining once again.
• During the April 2012 China Import and Export Fair (Canton Fair), cumulative exports fell by 4.8% and 2.3%, respectively.

Declines in Fixed Asset Investment
• Low investment demand as a result of low profitability of firms.
• The Four-Trillion-Yuan Investment consolidated the strength of SOEs while obscuring the prospect of private investment.
• Regulations in the real estate market may lower real estate investments, which may further lower investment demand in other industries.

Changes in Consumption
• Decreases in economic growth rate lead to declines in household income growth rate.
• The division of rural and urban economy, as well as imperfections in the social security system makes it more difficult for consumption to grow.
• The 2012 macroeconomic policies did not effectively raise consumption demands.

Decline in Liquidity
• Growth rate in foreign reserves has been declining. Mortgage financing from land and real estate is also declining due to strict real estate regulations.
• Decreases in growth rate of the real economy lead to declines in loan demand. The amount of new loans (medium and long-term loans in particular) issued remains quite small. This reflects low demand in fixed asset investment.
II. Future Trends:

In the Long Run, China’s Potential Economic Growth Will Depend On

- Changes in Labor Supply
- Changes in Capital Accumulation
- Changes in TFP Growth
- Changes in Environmental Cost

The Quantity of Labor Supply
- The quantity of labor supply will soon reach its turning point.
- The population growth rate kept declining after 2010, while the total working age population will peak in 2015.

The Structure of Labor Supply
- The total dependency ratio reached its lower bound in 2010, and will become larger and larger in the future.
- The increase of dependency ratio will lead to the rise of consumption and fall of investment growth rate. The growth engine of the economy will thus need to be transferred to consumption rather than investment.

The Increase of Resource Constraint and Environmental Cost
- The share of global resources China uses is increasing. Thus, China must increase its efficiency in energy use. The impact of resource constraint on economic growth is becoming more and more obvious.
- The environmental cost of economic growth is also becoming larger. For example, exhaust emission has been increasing since 2001. Moreover, the cost of pollution abatement is also increasing.
- China’s energy consumption per unit of GDP is not only larger than that of developed countries’, but it is also higher than that of India and Russia.

III. Major reforms needed

- Reforms in Land Market
- Reforms in Labor Market
- Reforms in Capital Market

Land Market Reform as a Way of Liquidity Injection
- Reforms are needed in the rural area to capitalize the land of the farmers, which means giving farmers full property rights to land and establishing a unified land market.
- This will be an excellent means of liquidity injection and it may also act as the starting engine for the next round of Chinese economic growth.
- Ownership registration and certification of the rural collective land, which already started in 2011, serves as excellent preparation for further reform.

Reforms in the Labor Market
- Reforms are needed to further promote urbanization and population agglomeration.
- Further reforms are needed in the social security and public goods sector, so as to eliminate institutional constraints such as the "hukou" system, as well as promote the urbanization process in China.
- By deepening reform in the labor market, population agglomeration will be more developed in the metropolis areas. The improvement of industrial organization, as well as the spilling over of technology and know-hows, will enhance TFP.

Two Major Problems in Chinese Financial Market:
- The capital price is not market based. Not only does this lead to the low efficiency of capital allocation, but it also exaggerates the impact of distortion of other markets.
• The development of capital market has long been devoted to the national economic construction dominated by the government, which is now confronted with more and more problems in the new social circumstances (i.e. in the population aging situation).

• Market-oriented and asset-management-based reforms are needed to ensure the sound development of Chinese financial market in the future. Financial efficiency can only been improved when the capital is combined with effective industries and young labor resources.

• Reforms in the financial market should encourage diversified participants in the financial market, promote multi-level development of the capital market, eliminate monopoly power and government intervention, balance the structure of direct financing and indirect financing, as well as enhance competition in the financial service sector, so that all kinds of structural imbalances can be eliminated.

Prospects of the Chinese Economy

• As a result of low external demand and difficulties in industry upgrading and domestic demand expansions, declines in economic growth rate in 2012 were inevitable.

• The present economic growth pattern is unsustainable. The Economic growth rate will reach its turning point in 2015-2016 unless factor market reforms and institutional reforms are implemented.

• If factor market reforms are implemented efficiently, domestic aggregate demand may expand, which will enable the Chinese economy to grow at a relatively high speed in the future.

THE END OF CHINA’S MIRACLE

Professor Hua Min, Director, Institute of World Economy, Fudan University

China’s economic miracle since 1979-GDP (0.1 billion)
Export in China Witnesses Rapid Growth Rate Since 2001, China's Accession to the WTO

The End of China’s Economic Miracle

The slowdown of China’s economic growth
The Consequence of the Real-Estate Bubble

Effect of Declining Export on Economic Growth

Reasons Behind the End of the Miracle

• Government Dominant Growth Mode
  – GDP worship
  – Bureaucrats control over domains hitherto belonging to entrepreneurs
  – Enterprises lack innovation

• Power Rather Than Contracts Determines Wealth Allocation
  – Lacks mature mechanisms that protect human rights and property rights
  – Traditional feudal culture

• Money Worship
  – Illegal production policies that violate human rights

• Conspicuous Consumption
  – Consumption that does not help improve spiritual richness

• Capital is Hoarded as Stock Capital
  – Large amounts of capital is hoarded in the real estate sector instead of the productive sector
China, a Country that Lacks Domestic Demand

Low Disposable Income Due to High Tax Wedge

Decreasing Rate of Employment Leads to Increasing Inequality

How to Tackle the Potential Crisis?

• Course—Return to Deng Xiaoping’s Idea
  – Opening to the outside world: facing the world, facing the future, get in line with international standards.
  – Reforms at home: market oriented or government dominant.
  – Development is an unyielding principle: solve the dual economic structure, reduce the rural population.

• Operation—Proper Economic Policy
  – Control the price of real estate.
  – Expand the real economy.
  – Stop structural readjustment, especially industrial upgrades.
  – Depreciate RMB.
  – Adopt expanding monetary policy and stringent fiscal policy.