

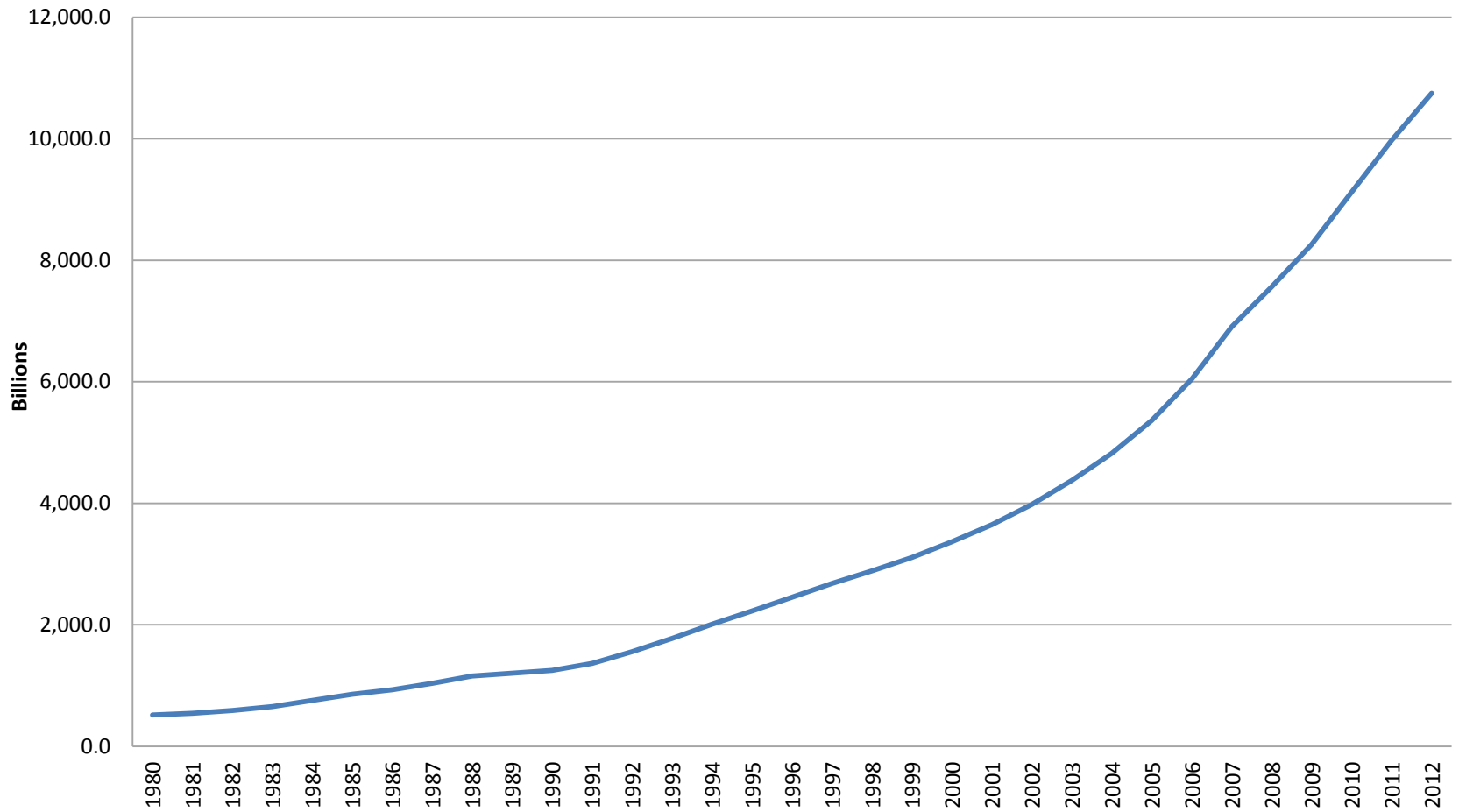
China's Economic Rise: Trends, Patterns, Challenges

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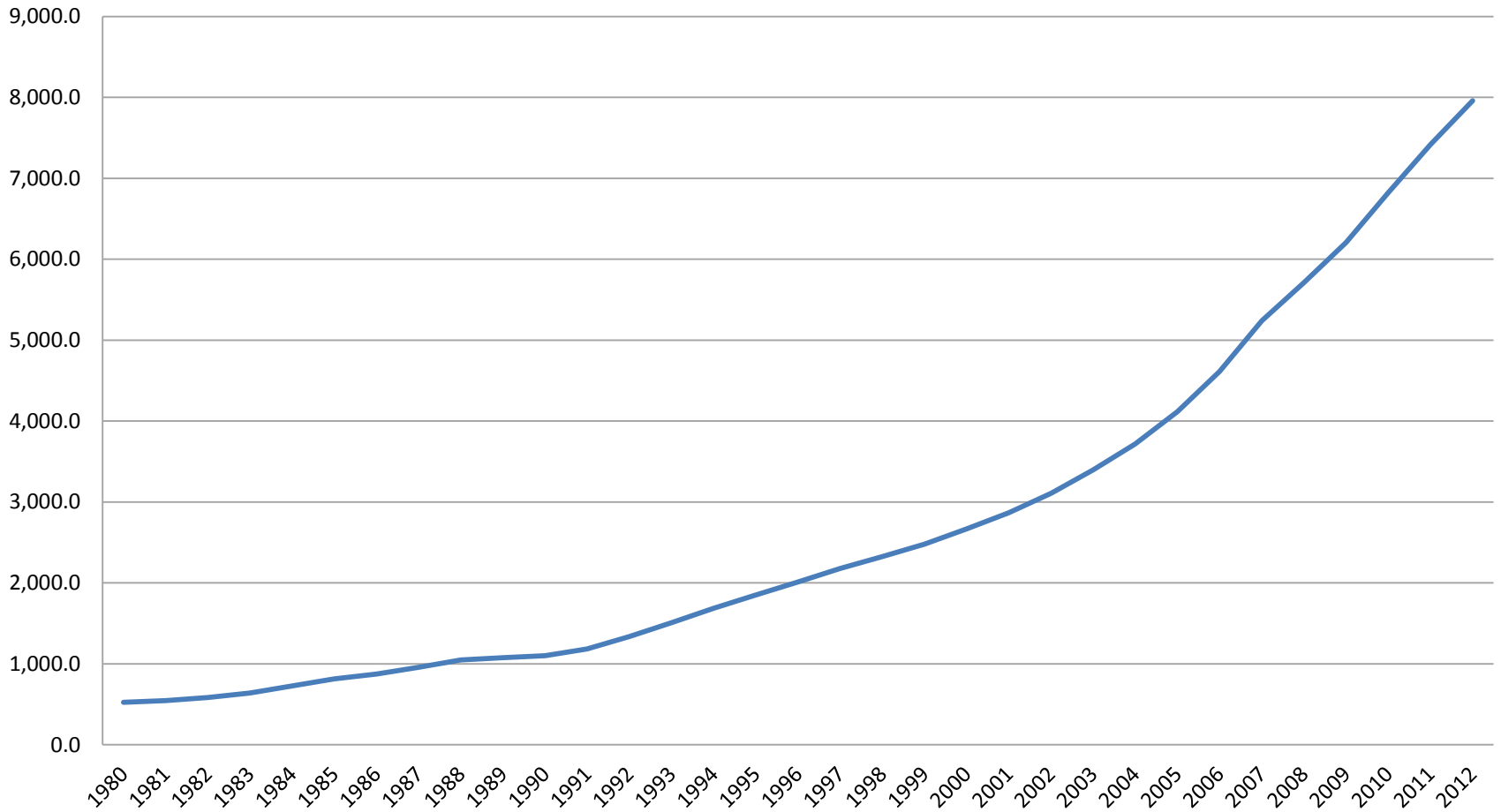
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China's GDP (in constant 2005 int. dollars)



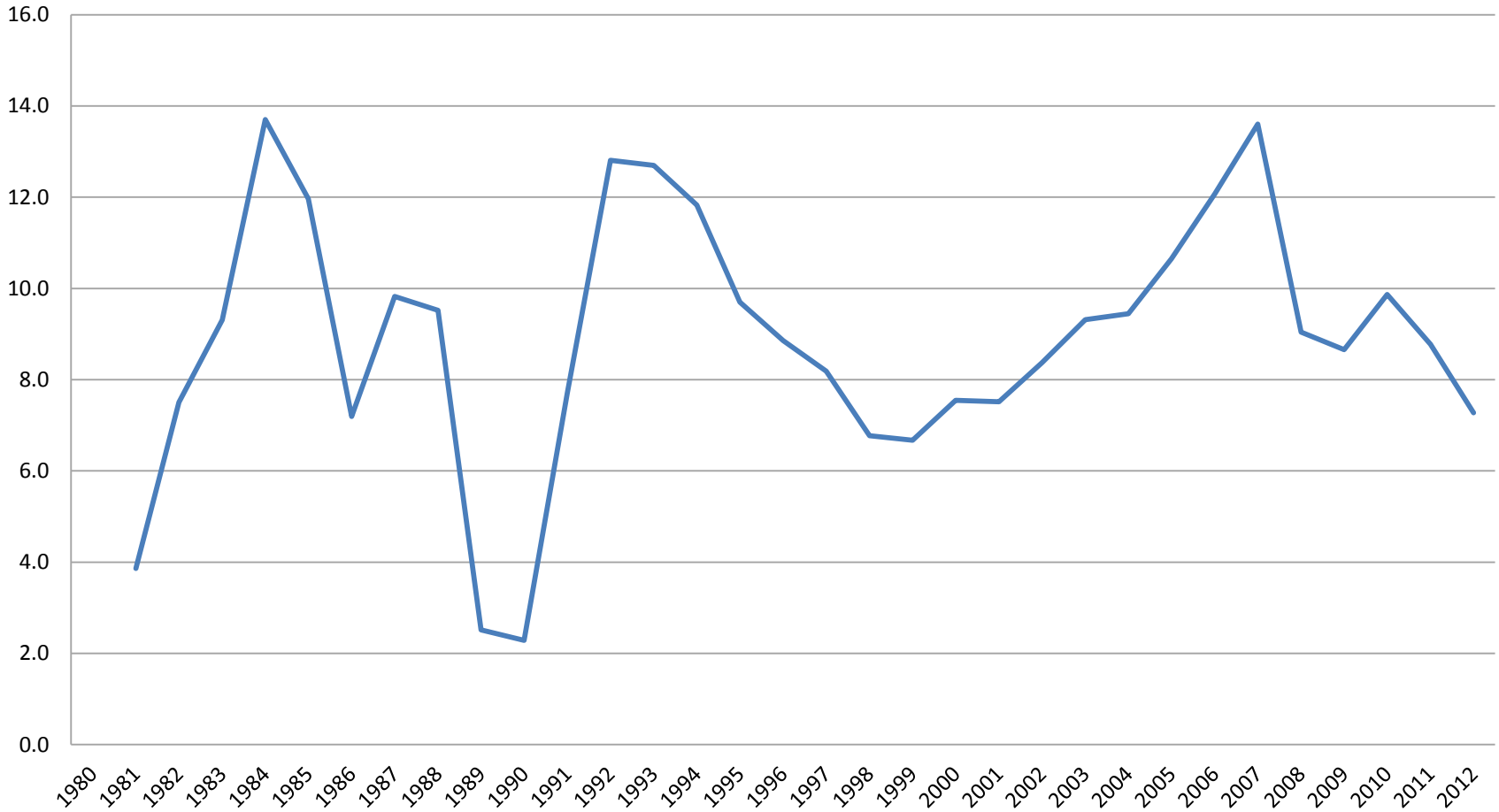
China's GDP per capita (in const. 2005 int. dollars)



Two key questions

- What has been driving economic growth in China?
- Can China maintain this level of growth in the long run?

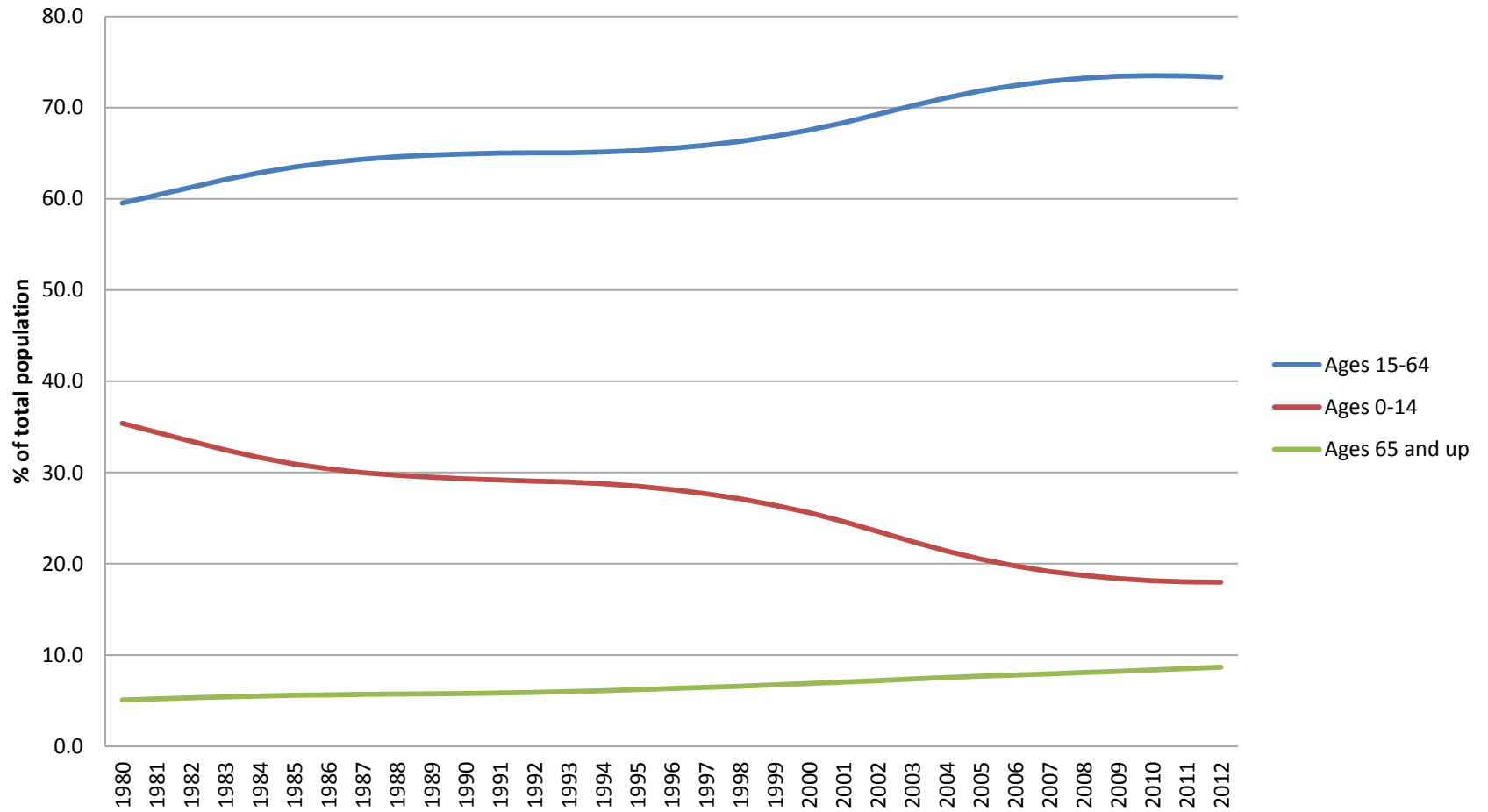
Growth Rate of China's GDP per capita (in %)



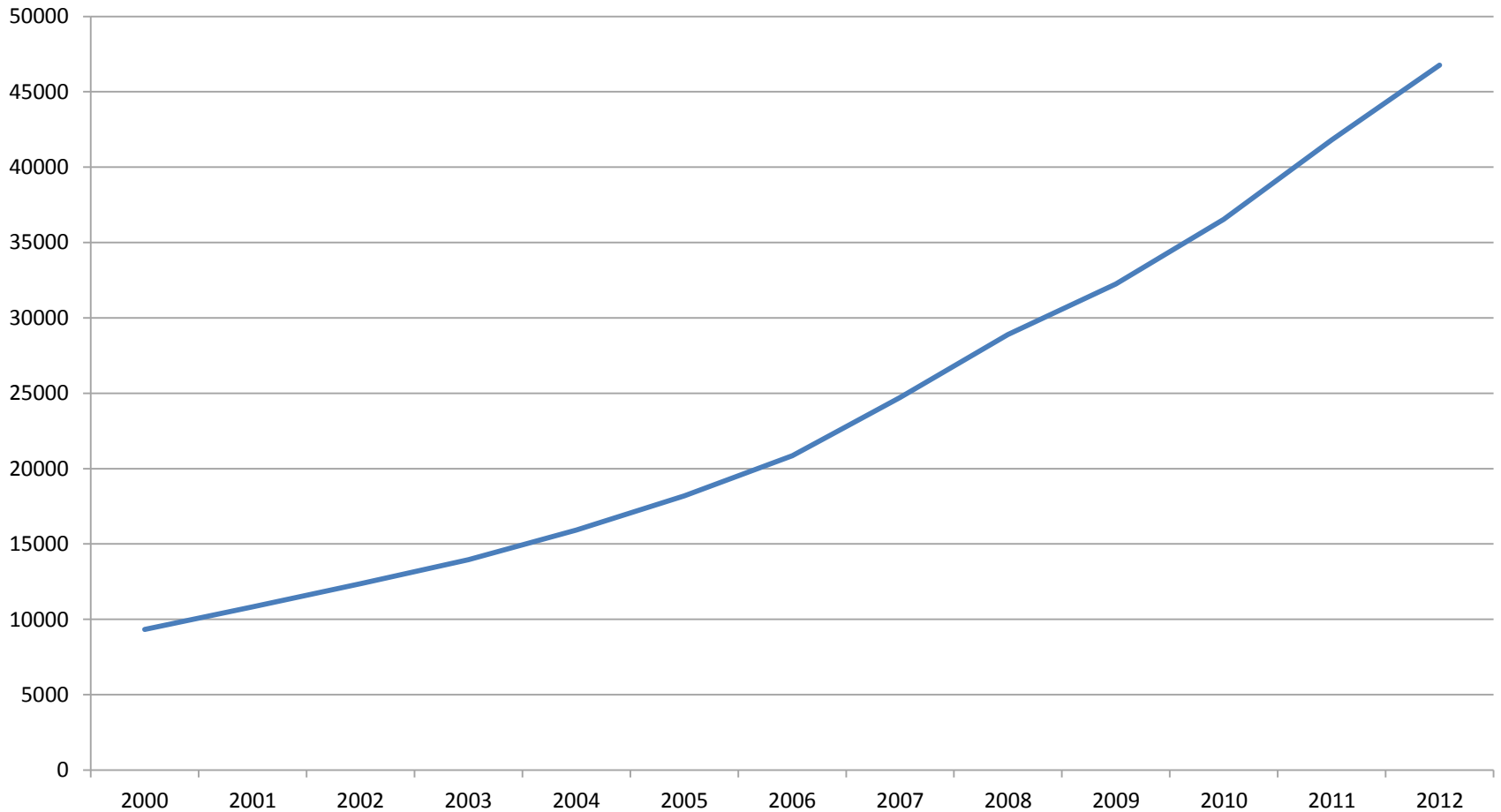
Demographic/Labor Factors

- Large share of working-age population
- One-Child Policy keeps population growth below 1%
- Wage repression keeps labor costs low
 - large pool of surplus labor in rural areas
 - no independent labor unions
 - administrative barriers in cities

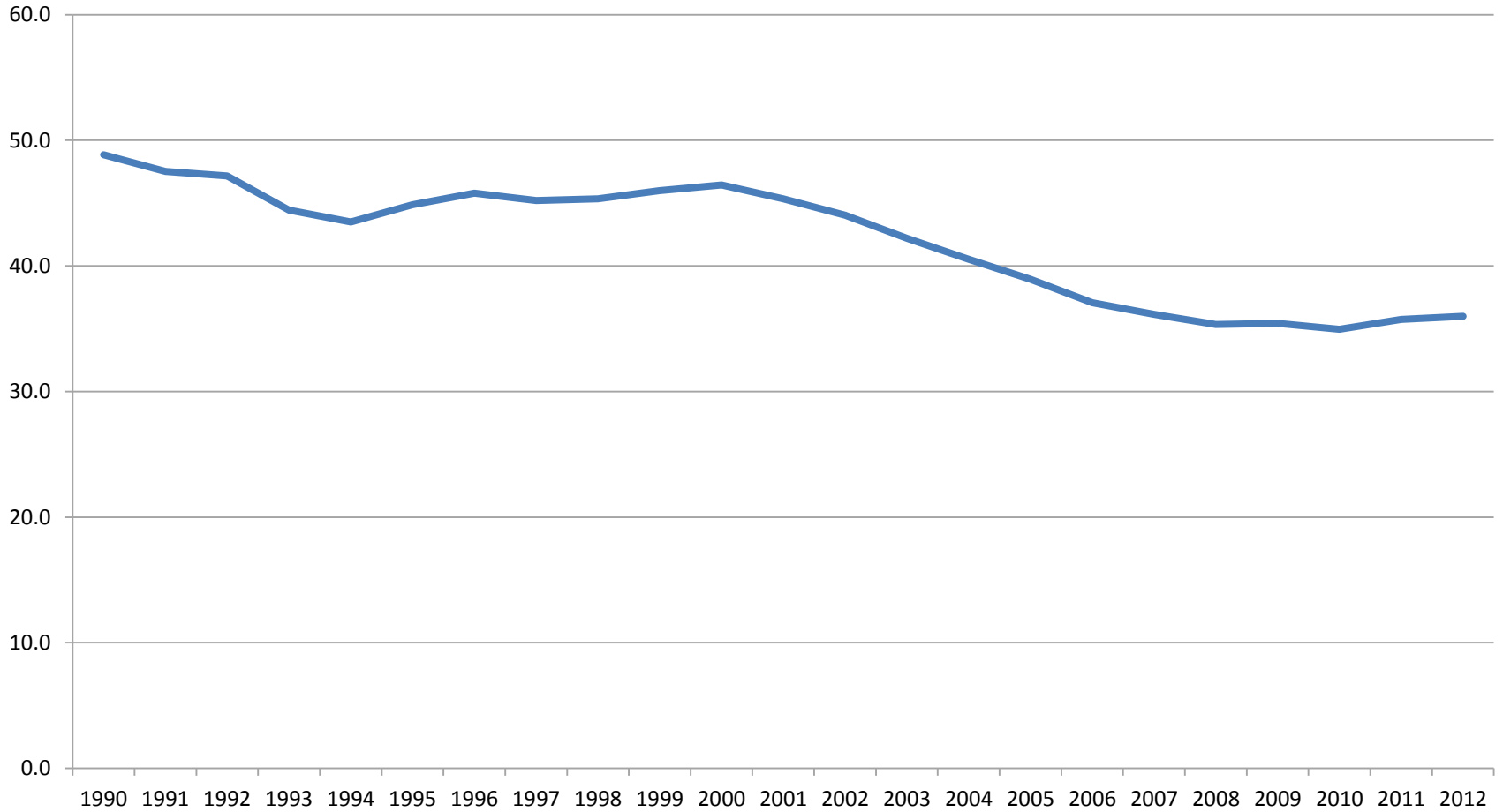
Population Share by Age



Wages of Urban Employees (in yuan)



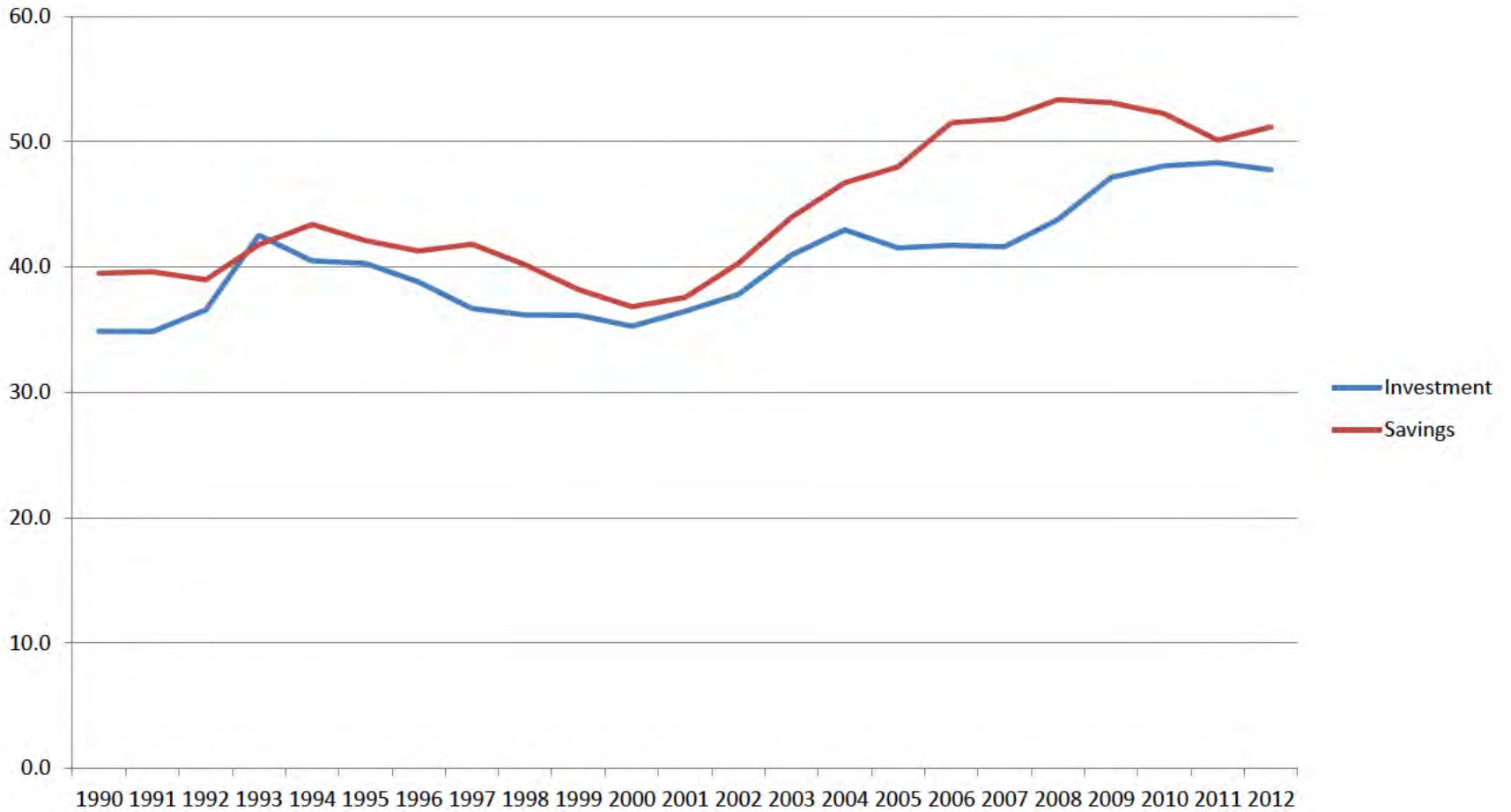
Share of Household Consumption in GDP (%)



Investment/Capital Factors

- Cost of capital kept low
- Government controls banking system and sets borrowing and lending rates
- Cheap capital channeled to large, mostly state-owned or controlled enterprises
- The result is a boom in investment, which in turn drives output growth
- Savers (households) and small, mostly private firms at disadvantage

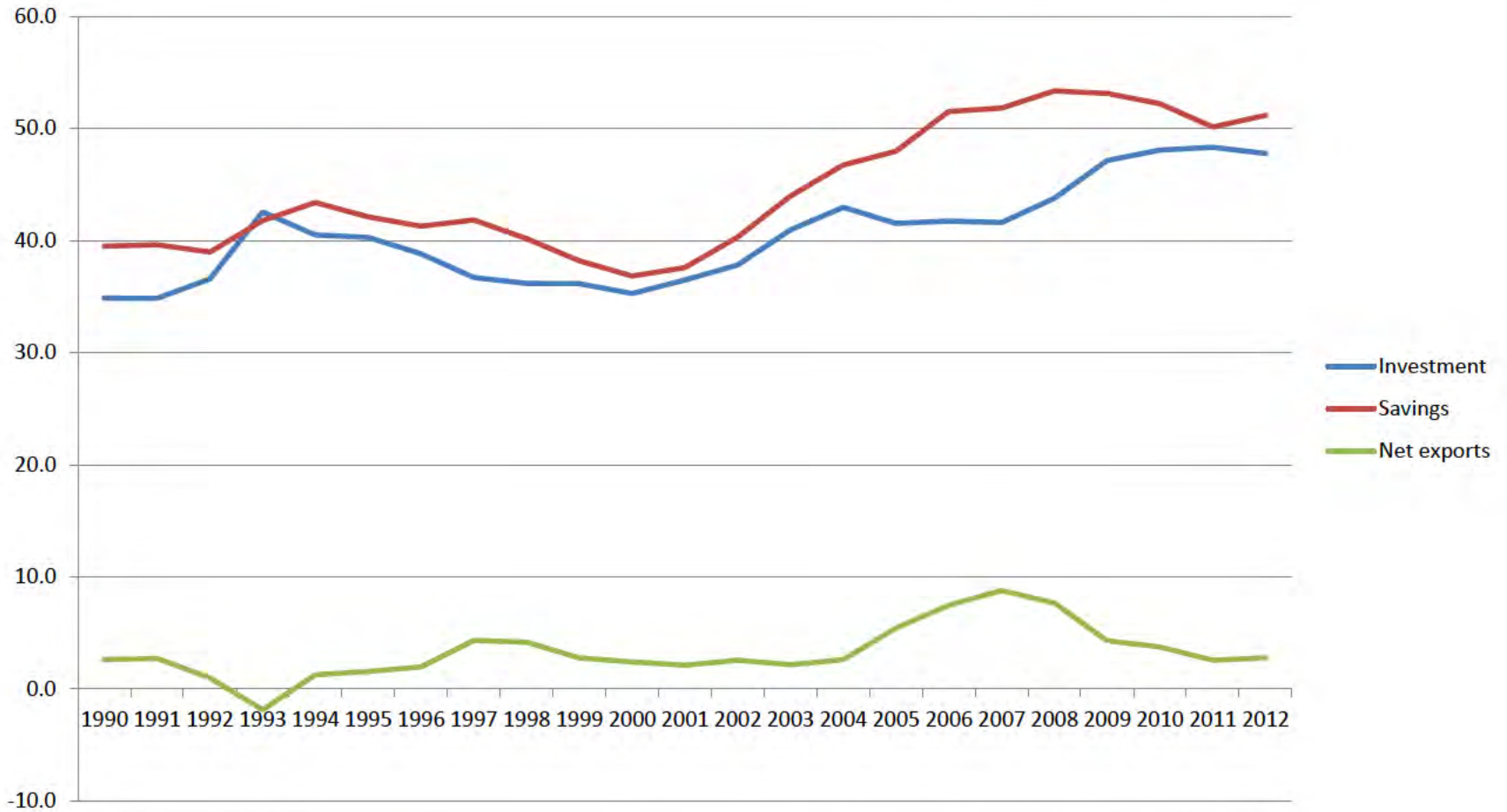
Investment and Savings (% of GDP)



International Trade Factors

- Repressed consumption and booming investment result in positive net exports
- Exports further boosted by an undervalued currency and various subsidies
- Strong foreign demand for Chinese goods produces large trade surpluses
- Undervalued currency further represses domestic consumption by households

Net exports (% of GDP)



Problems of Investment-based Growth

- Low cost of capital leads to misallocation
- More investment needed to produce the same increases in output
- Growing debt creates instability in the banking system
- Net exports vulnerable due to decrease in foreign demand in the aftermath of the recent global crisis
- Ageing labor force and rapid rise in wages

Rebalancing of China's Economy

- Double-digit growth rates are unlikely to be achieved again
- Gradual transition from an investment-based to a consumption-based economy needed
- Interest rates and exchange rates will have to be gradually liberalized
- Main danger is the collapse of the GDP growth rate if transition too abrupt