
Comment on Prasad: “Is Chinese Growth Built to Last?”

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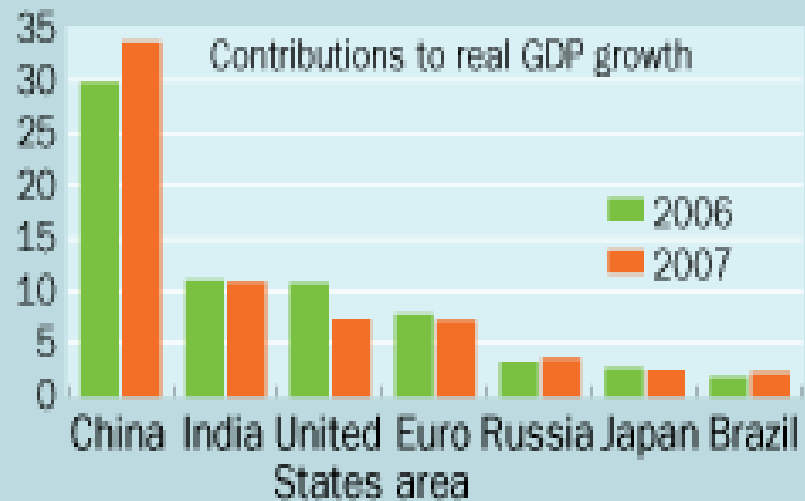
It matters to all of us

- China (along with the U.S. and India) has been the principal motor of global growth in recent years.
- If something goes wrong in China, everyone will know.

New driving force

For the first time, China and India are making the largest country-level contributions to global growth.

(based on PPP weights, percent of world growth)



Source: IMF staff calculations.

Key questions raised by this experience

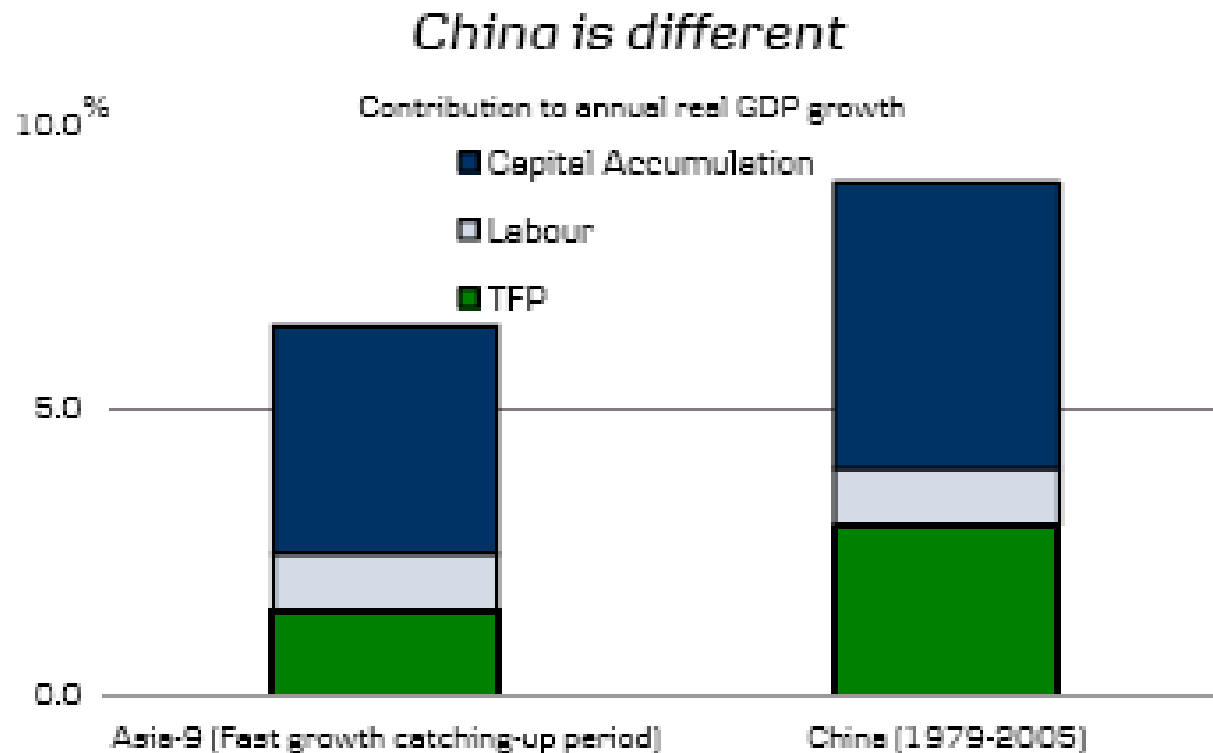
- Is there such a thing as a distinctive Chinese growth model?
 - Are the admirable results of that model sustainable indefinitely, or will China slow down, either gradually or with a bump?
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In my view, the Chinese model is not all that distinctive

- What China has done is to take the tried-and-true export-led growth model of late-developing Asian countries and pursued it with a vengeance.
 - The resulting pattern of growth has not been all that different from other Asian “miracle” economies.
 - Until recently, that is.
 - It is in the last ten years, when one would expect China to begin slowing down, that it has distinguished itself from its Asian predecessors by speeding up.
 - And this is where the questions of whether China is different, whether China can keep it up, and whether it might all come to grief appear in bold relief.
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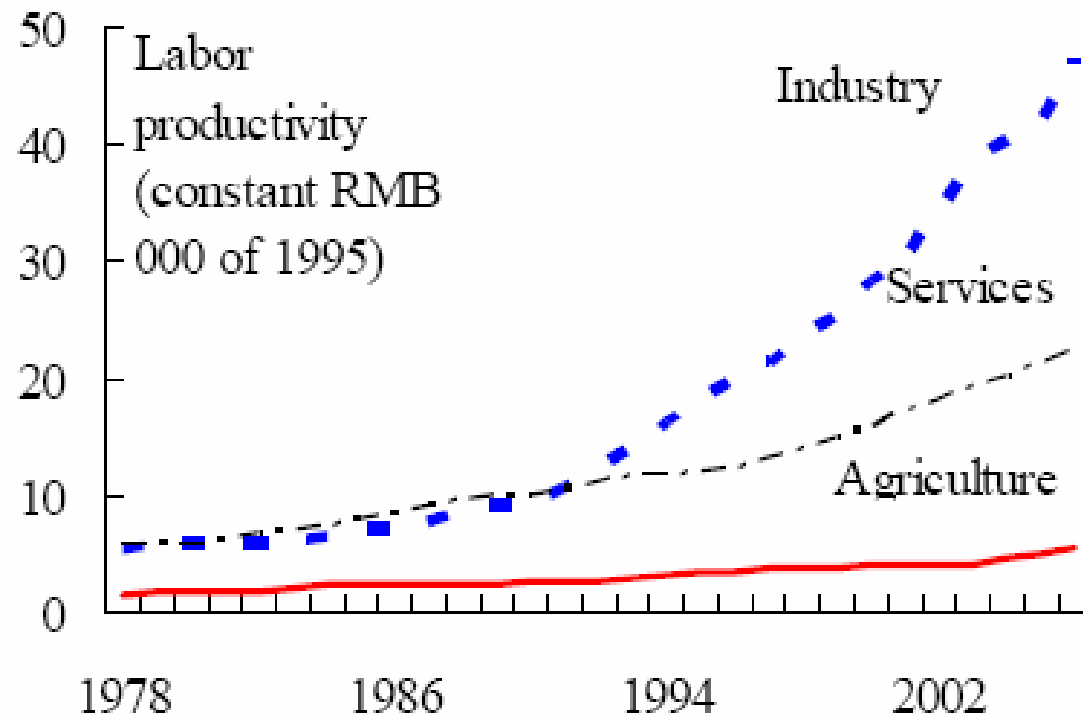
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- The next slides summarize the broad similarities between China and its Asian predecessors:

“China is different?” As in the predecessors the shares of TFP and capital resemble experience of NIEs



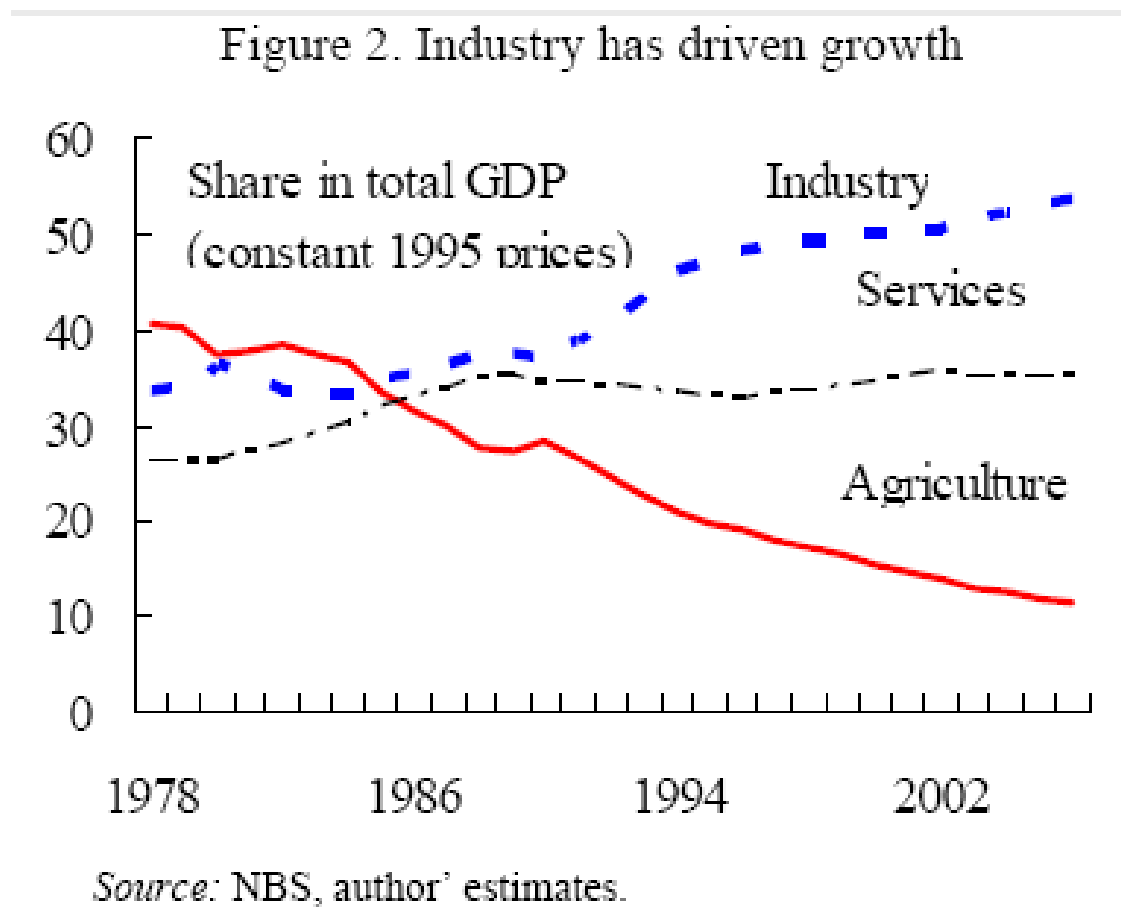
As in the predecessors, productivity is higher in industry than agriculture

Figure 3. Labor productivity in industry has soared



Source: NBS, authors' calculation.

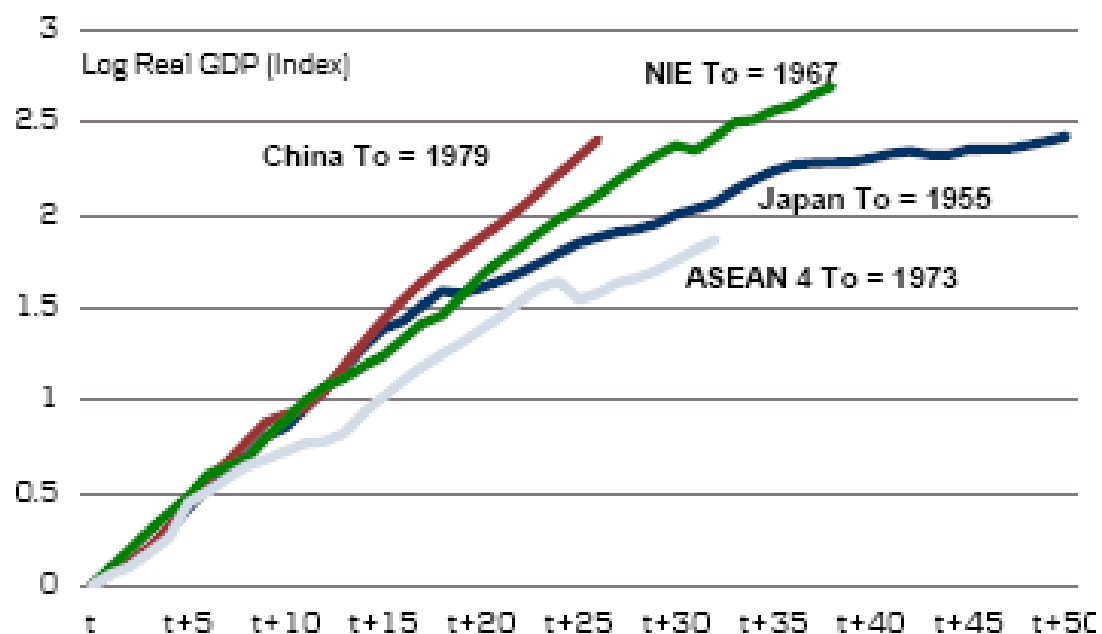
As in the predecessors, shifting labor from ag to industry has thus boosted growth



Cross country regressions can be used to make the essential points

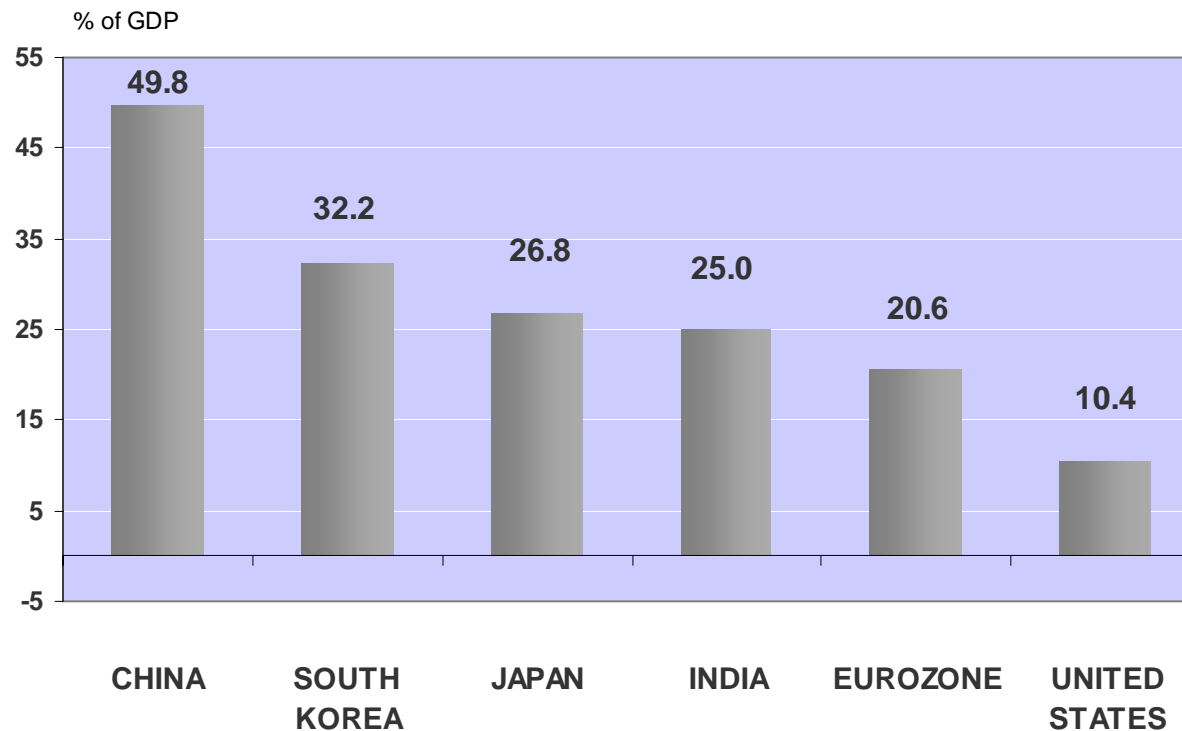
- A cross-country growth model can entirely explain Chinese growth from 1979 through 1995 by invoking:
 - initial per capita income,
 - favorable physical access to sea lanes
 - export orientation,
 - proportion of labor force in low-wage agriculture
 - stable monetary and fiscal policies
 - Implication: For more than 15 years, distinctive Chinese institutions and policy strategies added (and subtracted) little. They were neither the source of the country's rapid growth nor a barrier to it.
 - Subsequently, however, the model doesn't fit so well.
 - It predicts deceleration (as, inter alia, China's per capita incomes rise) where we observe acceleration.
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So what explains China's divergence in the last 10 years?

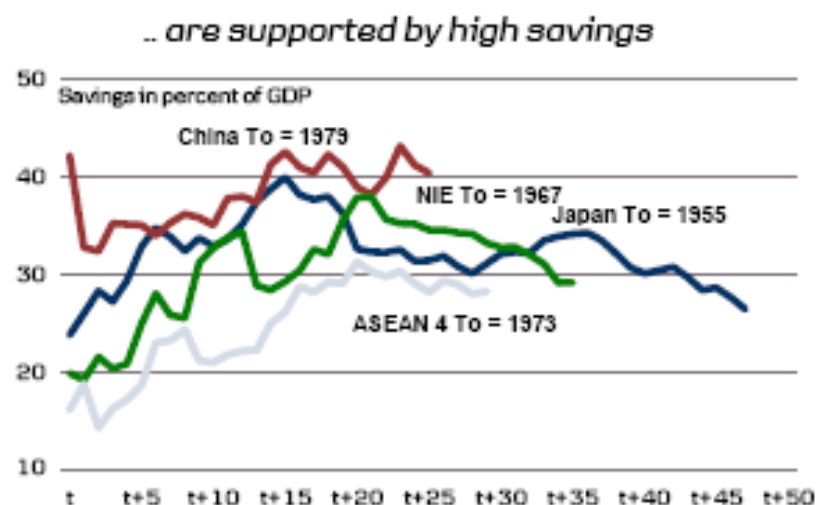
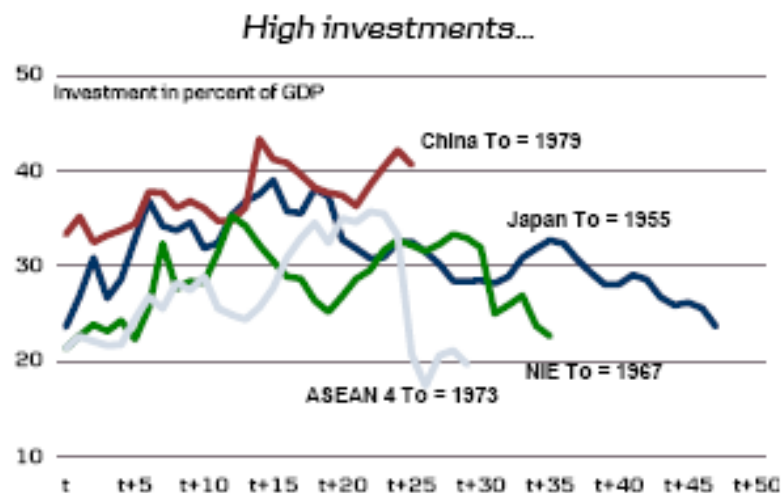


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- The macroeconomist's answer (naturally) would go as follows...
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Difference #1: China is running extraordinarily high savings rates (seen here is gross domestic savings)



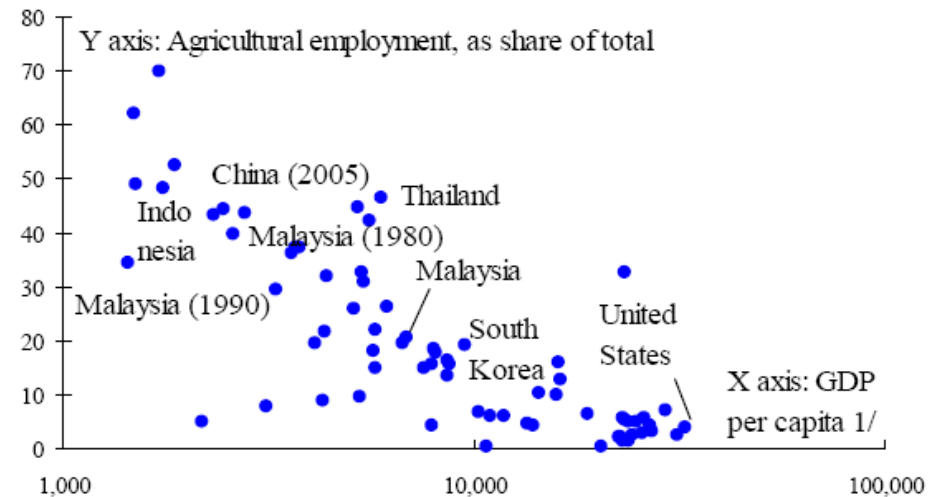
Difference #2: This has also made for higher than average investment



The question is: for how long is this savings-and-investment based growth model, emphasizing the shift of labor from ag to industry, sustainable

- In pursuing a model of export led growth sustained by a stable, undervalued currency and high rates of capital formation, China is following the same model as Japan, Korea, Taiwan, Hong Kong, and Singapore.
- China still has 200 m. underemployed workers in ag. If the overall economy grows at 10% a year, it can absorb 10 m. of them annually. So China can maintain its present model of extensive growth, which is supported by abundant supplies of cheap labor, for at least another two decades,

Figure 6. China still has a large share of employment in agriculture



Source: WDI, NBS, authors' calculation. 1/ 2001, unless otherwise indicated.

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- Or can it? Many things could go wrong. One could assemble a long list of possible problems (as the author does). To avoid these problems, China needs to:
 - **Close down loss-making SOEs.**
 - **Clean up the banking system.**
 - **Build strong securities markets.**
 - **Strengthen shareholder rights.**
 - **Address regional inequality**
 - **Clean up the environment**
 - **Reduce the energy and natural resource intensity of production**
 - **Address the inequality problem**
 - **Prepare for greater political contestation**
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- But it is not terribly helpful to say “many things could go wrong and should be fixed.” We need to prioritize, and Chinese policy makers should prioritize.
 - In fact the paper does this, and I tend to agree with its priorities.
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Most importantly, export-led growth could become more difficult

- Shortages of skilled labor and other nontraded inputs could develop. China could find it hard to move up the technology ladder into the production of more sophisticated goods.
 - The rapid growth of Chinese exports could produce a protectionist backlash.
 - Failure to share the fruits of Chinese growth more evenly could produce social unrest.
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- The solution to all three problems is a combination of currency appreciation with domestic measures to boost consumption and investment in nontraded goods sectors (education, vocational training, medical care, etc.)
 - Appreciation will address the concerns of potential protectionists abroad.
 - Measures to stimulate domestic consumption will prevent the economy from slowing as export growth decelerates
 - Investing in education, training etc. will relax skilled-labor constraints and allow China to move up the technology ladder into the production of more sophisticated goods and invest more effectively in R&D.
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There are many more problems, and all of these could be discussed in detail

- But your discussant has limited time.
 - For my money, it is on the nexus of currency/export/domestic demand issues on which policy reform efforts should focus.
 - And in this respect, the author has it right.
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- Thank you.
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