

The Economic Rise of China

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***The Economic Rise of China and India*, Accademia University Press, Torino, 2015**

China's economic ascent: GDP in PPP (US = 100)

Sources: Maddison (2007) , Conference Board (2016)

Countries	1870 GGDC GK	1913 GGDC GK	1950 GGDC GK	1950 GGDC EKS	1973 GGDC EKS	2015 GGDC EKS	2015 Ranking
China	192.9	46.6	13.0	9.5	11.8	108.7	1
India	137.1	39.0	15.3	10.3	9.0	43.1	3
United Kingdom	101.8	43.4	23.9	24.0	19.3	14.9	9
United States	100.0	100.0	100.0	100.0	100.0	100.0	2
USSR- Russia	85.0	44.9	35.0	35.0	42.8	20.7	6
France	73.3	27.9	15.1	15.3	19.6	14.7	10
Germany	73.3	45.9	17.4	18.6	29.1	21.4	5
Italy	42.5	18.5	11.3	12.2	17.8	12.1	11
Japan	25.8	13.8	11.1	11.3	36.0	26.8	4
Indonesia	19.2	8.7	4.6	5.1	6.0	15.8	8
Brazil	7.1	3.7	6.1	5.5	10.2	17.7	7

The Rise in China's Economy: Per capita GDP in PPP (USA = 100)

(p = preliminary estimates). Source: Maddison, Conference Board (2016)

Country	1870 GK	1913 GK	1950 GK	1950 EKS	1973 EKS	1990 EKS	2015 EKS (p)	Ranking 2015
China	21.7	10.4	4.7	2.6	2.8	4.6	24.8	9
India	21.8	12.7	6.5	4.4	3.5	3.8	9.9	10
United Kingdom	130.5	92.8	72.6	73.0	72.4	71.2	73.7	3
United States	100.0	100.0	100.0	100.0	100.0	100.0	100.0	1
Russia- USSR	38.6	46.8	29.7		36.3	29.7	43.5	7
France	76.7	65.7	55.1	54.9	81.0	77.0	70.8	4
Germany	75.2	68.8	40.6	41.4	78.2	79.1	84.6	2
Italy	61.3	48.4	36.6	39.5	68.7	75.8	62.6	6
Japan	30.1	26.2	20.1	20.6	70.1	82.9	68.1	5
Brazil	29.2	33.2	17.5	20.8	20.9	19.1	26.5	8

The economic reforms post 1978 and the *triple-mix* economy

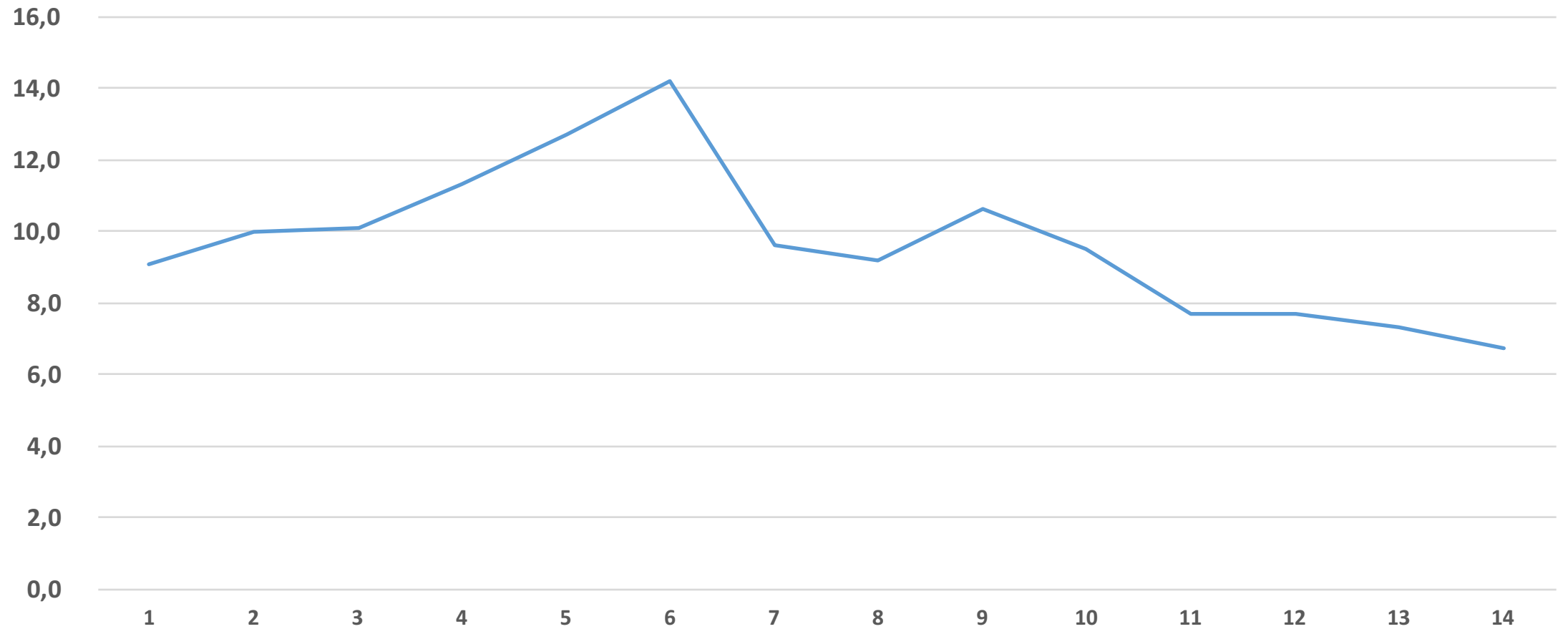
- **Plan => Market**
- **Public ownership => private ownership
of the means of production**
- **Centralization => decentralization
of main economic decisions**

The main present problems of China's economy

- **1) Strong slowing down of economic growth rate**
- **2) Rapid aging of the population**
- **3) Very high (and growing) level of pollution**
- **4) Difficult attempt to pass from an export-led growth to a growth mainly based on internal demand**
- **5) Rise in economic inequality and strong financial instability**

Figura 1: Real GDP growth rate in China: 2002-2015

(Source: OECD, 2015)



Why economic growth is slowing down ?

- **Combination of long- run structural causes, and medium- short- run causes, associated to the consequences of the global financial crisis 2008-14.**
- ***Structural causes:* progressive reduction of the advantages of *relative economic backwardness*, of *the fordist- toyotist model of growth* and of the accelerated industrialization; Increase of the importance of services, of population aging, of economic inequalities, of pollution and urban congestion costs, of financial instability.**
- ***Global financial and real crisis* => Reduction of the rate of growth of China's exports and of the level of inward FDI => reduction in the China's rate of growth of investment, consumption, aggregate demand, real GDP. Rise in outflows of Chinese FDI and portfolio investments.**

The consumption puzzle....

- After the global 2008-14 crisis and the strong slowing down in China's rate of growth, the Chinese government tried to rise internal consumption in order to compensate the weaker growth in exports. In 2007 the consumption rate (final consumption as % of GDP) was abnormally low (49,6%). There was so a strong stimulus package, and consistent wage rises (and even strikes) were allowed. Wages rose more than labour productivity. Moreover, the government tried to improve welfare (health, pensions and public services) for a part of internal migrant workers without *hukou*, i.e. the urban residence status. Finally, there was a strong rise in R.&D, infrastructure, military and anti-pollution expenditures, while the growth in industrial investments was attenuated.
- There was, however, an internal contradiction. Although the *consumption rate* increased a little bit, *the rate of growth of real consumption* decreased.
- This was essentially due to the fact that usually the rate of growth of productivity in industry is higher than the rate of growth of productivity in public services and welfare. Reducing the investment dynamics in industry, there is a reduction in overall productivity and GDP growth. Moreover, the trend towards maturity of some industrial sectors such as electric domestic appliances and PCs contributed to the the slowing down of growth. The fall in GDP and productivity growth led also to a fall in the rate of growth of domestic consumption and investment.

The instability in finance, housing prices and exchange rate

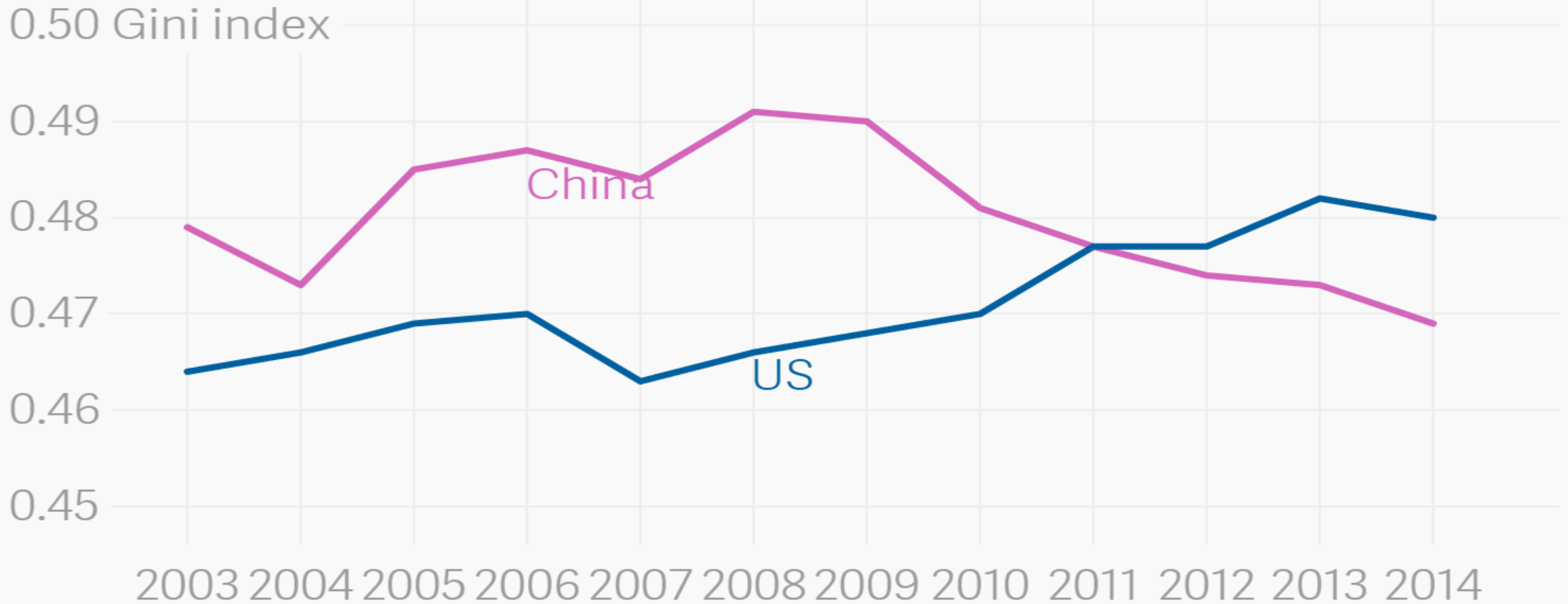
- In China there has recently been a phase of devaluation of the Chinese currency, and periods of falls in the stock exchange values and housing prices.
- The Yuan is fallen vis-a-vis the US dollar by about 9% from January 2014 to October 2016 and by about 12% versus the euro from April 2015 to October 2016. The composite Shanghai index is fallen by about 41% from June to October 2015 and then, after a partial recovery up to December 25, 2015, has again fallen by almost 24% up to the beginning of March 2016. The price index of housing is fallen for part of 2014 and 2015 and then has recovered since October 2015 up to now.
- However, these events must be seen in a wider historical perspective. For example, the recent devaluation of the Yuan has followed a period of almost nine years of considerable revaluation of the Yuan on the US \$ (about 27%).
- The fall of the Shanghai Stock exchange had followed a speculative bubble of about 150% from July 2014 to June 2015.
- The price of housing had a strong rise in 2012 and up to November 2013.

Long-run determinants of financial instability

- In order to understand the long-run determinants of China's financial instability, we must consider, besides the important changes in economic policy since 1978 (tolerance and then recognition of private property, etc.), the peculiar evolution of China's economy.
- Income inequalities have rapidly risen from the 1980s up to 2008, diminishing a little bit since then (see Figure in next slide). Probably wealth inequalities between the very rich and the very poor have continued to grow also in recent years. The saving stock of households has enormously increased, thanks to the very high saving rate and the rapid rise in income. The private sector of the economy has rapidly grown since the mid-1990s and the number of very wealthy people has enormously augmented.
- There has been, thus, an important relation between a stock (wealth) and flow variables (GDP, consumption, investment, etc.), while in the meantime there has been a progressive relaxation of the rules and constraints imposed by Chinese authorities to the financial and housing markets and to some capital international movements.
- In 2015 China's national wealth was over three times the GDP and the richest 1% owned about one third of national wealth. If, as it happened in the period 2013-16, wealth rapidly rises and then briskly falls because of speculative bubbles and busts on the prices of shares and buildings, there can be enormous destabilizing effects on the economy, contrasted with increasing difficulties by China's authorities.

The official Gini income distribution index in China and in the US

Inequality in China is less than it is in the US, officially



△ T L △ S | Data: National Bureau of Statistics of PRC, US Census Bureau

The impact on the European Union - 1

- Even if the rate of GDP growth in China is gradually slowing down, it remains about *four times higher* than that of EU (in 2015: 6,8% versus 1,6 %).
- In 2014 *EU was the top importer* of goods from China (302 billion euros) and *the second highest exporter* towards China (165 billion euros). EU had so an *enormous commercial deficit* (about 137 billion euros), mainly depending on manufactured goods. This deficit has diminished from 2008 to 2015, because of the growth of net EU exports partly due to the depreciation of the euro on the Chinese currency from April 2012 to March 2015. As regards services EU has maintained a modest surplus.
- As to FDI, EU conserves a positive net balance in terms of outward minus inward FDI stocks, but in the 2000s China has very rapidly increased its outward FDI stock towards EU. The latter are principally directed towards Germany, France, United Kingdom, Netherlands, Austria, Italy.

The impact on the European Union - 2

- **The slowing down of economic growth, China's rising unit labour cost per product and its greater financial instability might have mixed effects on EU's economies.**
- **On one hand, China's slowing down reduces the world economic demand and so increases EU's difficulties.**
- **On the other hand, China's slowing down has contributed to the diminution of the price of oil and other raw materials, before pumped up by the rapid growth of China's demand.**
- **The growth of economic and financial interconnections between China, the US and EU and the rise in financial and exchange rate instability in China might increase world financial and economic instability.**
- **The rise in unit labour cost per product in recent years in China may reduce the competitive pressure of China on EU countries. Countries as Germany and other EU Nordic countries, which have continued to massively invest in knowledge and have made relevant FDI in China have so acquired a good penetration in its enormous market.**

The impact on Italy -1

- Italy, as other EU countries might be influenced with mixed effects by China's slowing down and its growing financial instability.
- In 2015 there has been a reduction both in Italian exports to China and in Italian imports from China. There has been so a further rise in the enormous Italian trade deficit towards China, which had instead diminished from 2010 to 2013.
- In recent years, also because of the relatively low prices of the shares of our principal corporations, there has been a rapid rise of Chinese acquisition of Italian firms.
- Including also Hong Kong, China has, for example, bought: Tre Italia (about 13 billion euros), a terminal in the port of Taranto (Hutchinson Whampoa - Hong Kong); Pirelli (Chem China) for about 7 billions euros; 35 % of CDP reti (State Grid Corporation), 40% in Ansaldo energia (Shangai Electric Group), Krizia, Fiorucci; 8% in Ferragamo; Ferretti, Benelli motorcycles; some design firms; even two soccer teams (Milan and Inter), etc.
- People's Bank of China has bought over 2% of the shares of Fiat, Telecom, Prysmian, Eni, Enel, Generali, etc. Several large Chinese corporations has opened branches in Italy. Although also several Italian firms have made relevant FDI in China, the overall balance is shifting in favour of the Asian economic giant.
- We must also notice that there are over 320, 000 Chinese immigrants in Italy who send in China remittances for about 2-3 billion euros per year. These immigrant often come from the zone of Wenzhou, and many of them have opened small and medium size firm (textile, restaurants, coffee shops, etc.).

The impact on Italy- 2

- China represents a *problem, but also a great opportunity* for the Italian economy.
- We are well present in China for capital goods and in the luxury and fashion industry, both with exports and FDI joint-ventures. We are rapidly re-enforcing exports and FDI in the agricultural, quality wine and food industry, though with a strong delay with respect to countries as France. Also in the attraction of Chinese tourists Italy is badly outperformed by France, though is trying to catch up.
- The automobile corporation Fiat, now FCA, has not been as successful as German, Japanese, American and South Korean groups in entering the Chinese market, which is now the world largest. Fiat has then changed partner in its joint-venture with Chinese firms, while for trucks Iveco has done somewhat better.
- In China, in order to operate with profit, it is necessary great patience, deep knowledge of the local culture and careful building of medium-long term relations.
- Some medium size or big firms have been successful. Small firms, poorly assisted by the system-Italy and usually unable to create well functioning consortiums and to fully utilize e-commerce, have often failed. A better collaboration with Italian banks operating in China, ICE, SACE, Chambers of Commerce and Italian institutions abroad would be very important,

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- OEET (*Osservatorio sulle economie emergenti-Torino- Center on emerging economy -Turin*), directed by Mario Deaglio, Giovanni Balcet e Vittorio Valli, has detailed notes and analyses on China and other emerging economies. <osservatorio-economie-emergenti-torino.it> (open access).