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CEPN Policy Brief

Economic slowdown: China in turmoil?

Pierre SALAMA

Abstract : “It doesn't matter whether the cat is black or white, as long as it catches mice.” With the slowdown in growth, the proliferation of labour disputes that are increasingly difficult to control and the struggles of small farmers to uphold their rights, it is likely that in the future, China will find it ever harder to “catch the mouse”.

Measured at the current exchange rate, China's per capita GDP increased by a factor of more than 22 between 1980 and 2011, rising from 220 dollars in 1980 to 4930 dollars in 2011. Expressed in purchasing power parity (PPP), it grew by a factor of 33. Thanks to very high long-term growth with little volatility, there has been a substantial reduction in poverty. However, the rapid widening of income inequalities partly offsets the positive effects of strong growth on the reduction of poverty, which continued, but at a slower rate.

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I. The originality of the Chinese model

The originality of the Chinese model lies in its capacity to unite fire and water: socialism and the market economy. The private sector has developed strongly, and is not limited simply to the

activities of multinational companies. The public sector is very important. Its modernisation is financed by very low-interest loans, at the risk of exerting “financial repression” on the private sector, which has to borrow at high interest rates. Public enterprises benefit from large subsidies. Protected by administrative measures and the maintenance of a depreciated exchange rate, the prices of manufactured goods are increasingly free. However, there is less liberalisation in the case of intermediate goods, which benefit from numerous subsidies. It is limited for factors of production, notably as regards raw materials, credit conditions and labour, the prices of which are maintained at low levels. Lastly, China can be characterised by the facilities provided for the purchase of foreign companies (with the aim of appropriating the most recent technologies), by a certain protectionism, through the maintenance of a depreciated exchange rate and the de facto exclusion of foreign companies from public calls for tender.

The originality of this model is based on:

- the articulation of social forces under the auspices of the Communist Party: entrepreneurs in the public and private sectors who are usually members of the Party, a labour market with increasingly marked differentiations between town and country, skilled and unskilled workers, resident workers, and rural migrants (mingong) without residence permits (hukou) who have very few social rights. There are 260 million of these rural migrants, concentrated in tough, unskilled jobs;
- the capacity of the central government to maintain control over the provincial governments, political concentration and the relatively low level of autonomy with respect to the central authorities;

Directeur de la publication : David Flacher, Directeur du CEPN

Rédacteur en chef : Nathalie Coutinet | Maquette : Philippe Abecassis

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China: some salient facts

	1980	1985	1990	1995	2000	2005	2011
per capita GDP at current exchange rate	220	280	330	530	930	1740	4930
per capita GDP at PPP	250	500	800	1480	2340	4090	8430
Poverty rate (less than 2 dollars PPP/day in %)	98	93	85	74	61	37	30

Source: World Bank-World Development Indicators, *on line* (July 2012)

- high growth that can be used to justify the continuation of an authoritarian regime, despite the particularly unequal distribution of the benefits of growth and the rise in corruption.

Massive State intervention, the vulnerability of private and public entrepreneurs, corruption and the overexploitation of workers, especially those without official papers, are the particularities of this model¹. In fact, there are two processes of primitive accumulation at work here: one in the sense of Marx, with the flow of rural poor into the cities, the second more complex, with the dispossession of savers through very low or even negative interest rates, and the granting of low-interest credit to selected public and private companies.

II. A combination of unfavourable factors leading to a more pronounced slowdown in economic activity

1/ The prospects of strong growth in exports are much weaker than in the past, all the more so since it is increasingly difficult to move from a specialisation based on the export of low-tech products to more sophisticated goods with greater added value. Upstream industrialization faces two daunting obstacles. Firstly, with globalisation, it has become harder to oppose the international fragmentation of the value chain, and secondly, the lack of mastery of the new technologies, notably those relating to telecommunications and information, combined with the absence of know-how, make it difficult, but not impossible, to implement national strategies of upstream industrialization and integration of production lines.

2/ Changing from one model of development to another, based on the dynamics of the domestic market, is not easy, despite the growth of the middle classes. Admittedly, wages have on average risen faster than labour productivity since 2009, but the share of consumption in GDP and its contribution to growth are still increasing too

slowly. The rise in labour costs for a given rate of labour productivity growth, following that of incomes, reduces the competitiveness of labour-intensive companies. Growth in consumption could still be driven by dissaving. The high level of household saving – due to precautionary behaviour motivated by the costs of health care and education, inadequate pensions² and job insecurity – could be reduced if there were more substantial mechanisms of socialization, requiring a large increase in the social spending of the State.

3/ Many of the investments are dedicated to important infrastructure projects. These are a prerequisite for long-term growth, and their absence explains the difficulties encountered by both Brazil and India in maintaining strong growth. But in China these investments are largely responsible for the proliferation of bad debts that weaken the banks. At first glance, one might think that despite these bad debts, the financial and banking risks are not yet too high in China, since the credit-to-GDP ratio was 154% in 2012, lower than that of the United States on the eve of the 2007 crisis (224%) or that of Japan before it ran into difficulty in 1989 (239%). In fact, however, one must also take into consideration the complex financial products, in other words all the shadow banking activities performed by financial institutions, which are very little controlled by the monetary authorities, and their relationship to the banking system. These activities increased by 62% between 2008 and 2012, and when they are taken into account, the credit-to-GDP ratio rose from 145% in 2008 to 207% in 2012, according to data from Nomura International. So the risk of a financial crisis and hard landing is higher than it might appear to be when one only considers credit, excluding complex products from the equation.

4/ Excessive rates of investment (43.5% in 2010) cause additional costs deriving from substantial idle production capacity. With such high investment rates, capital efficiency tends to diminish, especially among State enterprises and the real

¹ Although wages have risen sharply in recent years in China. According to the ILO (2012, p.25), the average annual growth rate of wages was 13% between 1997 and 2007 and 11% between 2008 and 2011, while the average annual growth rate of productivity in the same periods was 9% and 8.5%. Wage inequalities are on the increase, with the wages of unskilled workers, especially those of undocumented migrants, rising more slowly than the growth rate of the economy, the pool of labour not being unlimited.

² The dependency ratio is rising sharply because of increasing life expectancy and the single child policy.

estate sector, weakened by the possible bursting of a speculative bubble.

5/ Controlling social conflicts while at the same time maintaining the supremacy of the Chinese Communist Party is all the more problematical because of the opacity of government decision-making and the amount of corruption at all levels.

- The impact of an economic slowdown on the international prices of raw materials and the volumes traded is already being felt by the emerging Latin American economies and numerous African countries. If China's growth were to fall markedly, the economic consequences for these countries as well as the developed countries would be even greater, and this would in turn reduce the growth of Chinese exports.

Conclusion

More than a "hard landing", it is social conflict, fuelled by the fall in growth, which threatens the continuation of the political regime. Unable to maintain strong growth in wages or reduce wage inequalities, the government seeks to avert social conflict by planning to give way on a number of qualitative elements: recognition of property rights for small farmers, recognition of the validity of some of the demands of workers, introduction of a social security system, protection of the severely degraded environment, and lastly a "fight" against the corruption affecting political staff and business executives at all levels.

For Chinese economists and political scientists, the authoritarian regime is not based on its ideological legitimacy but on its effectiveness. As Deng Xiaoping put it: "It doesn't matter whether

a cat is black or white, as long as it catches mice". With the slowdown in growth, the proliferation of labour disputes that are increasingly difficult to control and the struggles of small farmers to uphold their rights, it is likely that in the future, China will find it ever harder to "catch the mouse".

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Seminars & Conférences

12 déc. 2013 – 17:00-19:00 - Université Paris 13, campus of Villetaneuse -Room K303

CEPN-OSIRIS Séminar

DAMIEN BESANCENOT (CEPN), JOÃO FARIA (University of Texas at El Paso) & KIM HUYNH (Bank of Canada and Indiana University) :
"Congestion of academic journal under papers' imperfect selection"

13 déc. 2013 – 14:00-17:00 – Maison des Sciences Économiques (Paris)

Health Political Economy Seminar (STRAS group)

BERNARD FRIOT (Institut Européen du Salarat et IDHE)

"Financer la couverture santé par une hausse de la cotisation ou par un mixte CSG/régime complémentaire professionnel ?"

16 déc. 2013 – 8:30-17:30 - Vietnam Academy of Social Sciences (VASS), Hanoi

International conference : Regional Integration, Inequalities and Social Cohesion in East Asia

Co-Organised by CAF Hanoi, CEPN, DIAL, IRASEC, UNESCAP.

18 déc. 2013 – 9:30 -18:00 - MSH Paris Nord - Conférences Room

Seminar/Workshop: Vers de nouveaux cadres de représentation du développement durable ?

Co-organised by CEPN (Pascal Petit & Hélène Tordjman) and the Chair of the Global Studies College (Dominique Méda)

19 déc. 2013 – 12:45-14:00 - Université Paris 13, Campus of Villetaneuse -Room K301

CEPN Lunch seminar on Political Economy

CÉDRIC DURAND (CEPN)

"Weird capitalism: Financialization, globalization and the profits without accumulation puzzle"

20 déc. 2013 – 14:00 -16:00 - MSH Paris Nord –Conférences Room

CEPN Séminar

ISABELLE MEJEAN (École Polytechnique)

"Low wage Country Competition and the Quality Content of High-Wage Country Exports"

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National Polytechnic School of Oran (ex: ENSET) - Oran (Algeria), 24-25 June 2014

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New Books



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ERICK LEROUX, PHILIPPE CALLO (eds) – 2013 –L'HARMATTAN

Sustainable tourism must meet the tourists and give them a unique but also useful in raising awareness of sustainability issues and encouraging them to adopt best practices experience. Remember that the inclusion of sustainable development began with the creation of regional or national parks. The hospitality professionals, hosting and tour operators now offers sustainable tourism products. Sustainable tourism therefore requires the establishment of practices and sustainability criteria, and management of tourism employs.

With contributions from: Isabel Babou, Patrice Ballester, Mireille Barthod-Prothade, Philippe Callot, Bruno Cardinale, Cécile Clergeau, Frédéric Desglis, Mbaye Fall Diallo, Xavier Dupuis, Sall Fatou Diop, Luc Florent, Christian Germanaz, Thi Thuy Duong Ha, Aziz Hmioui, Erick Leroux, Jean-Bernard Marsat, Béatrice Moppert, Krystal Paulus, Olivier Saissi, Michel Sicre.