China's Economic Development and its Contribution to the World

By Nishimuro Taizo

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Introduction

China achieved high economic growth rates throughout the 1990s and has maintained annual growth of 7 to 8% even since the year 2000. The temporary slowing of the U.S. economy brought about by the collapse of the information and communication technology (ICT) bubble in 2001 dampened growth in the newly industrializing economies (NIEs: South Korea, Taiwan, Hong Kong and Singapore) and the Association of South-East Asian Nations (ASEAN), but China shrugged off the impact and maintained a growth rate of 7%. China's accession to the World Trade Organization (WTO) in 2002 spurred its imports and exports, which increased more than 20% compared with 2001, and the country's impact on the global economy has grown.

In addition to the expansion of China's domestic market, foreign trade and foreign direct investment (FDI) have underpinned China's remarkable and rapid progress. In 2002, FDI in China surpassed $50 billion, more than that of any other country. This massive investment has spurred continuous expansion of China's exports, prompting renewed debate on the revaluation of the *renminbi* (RMB) in the United States, Japan and the rest of the world.

In light of the history of the international currency system, it is clearly desirable that countries have stable exchange rates. Although foreign currency exchange rates are influenced by countries' economic fundamentals, a certain level of flexibility is desirable from the viewpoint of the global economy. This is because unstable exchange rates not only influence domestic economies, but also tend to have an immediate impact internationally.

Today, I would like to offer my views on several issues. The RMB, which is currently the subject of much discussion between the United States and China, and Japan and China, is of course one of those issues. I would also like to make comments on the Chinese economy and its future direction, and on what China needs to do in order to fully integrate itself into the global economy.

The Present State and Problems of the Chinese Economy

High growth rates and the ability to attract investors from around the world paint a picture of a China making progress in all directions and on every level. A more considered look reminds us that it is important to note that China also has various problems. I would like to call attention to them and comment on the most important ones.

First and foremost are the increasing disparities in wealth and rising unemployment. China has to cope with simple income differentials, as well as regional differentials. For instance, the government has been endeavoring to develop the midwestern region, but the general drift of the population is to the larger cities. It is necessary to examine whether attempts to develop the regions will be successful and how China will cope with the growing migration to the big cities.

State ownership of enterprises remains a major issue, a number of issues in fact, including the bad debt held by China's banks, government expenditures and the increase in government debt. According to some observers, banks' bad debts account for as much as 50% of loans outstanding, the national budget deficit is ballooning, partly due to increasing investment in infrastructure, and government debt exceeds GDP by more than 100%.

While an annual growth rate of 7-8% is impressive, it has to be set against a high rate of population growth. Despite the government's efforts to impose a one-child policy, China's population has increased by 300 million in the past 10 years, an extremely fast growth rate. In order to support this level of population increase, China will have to maintain current levels of economic growth far into the future.

In addition to the expansion of the domestic market of China itself, FDI and exports have been underpinning China's growth. We know that FDI for this year exceeds the level of $50 billion. Additionally, continued increases in exports from China fueled by FDI will only stimulate more debate on the revaluation of the RMB. Moreover, export expansion is always accompanied by the possibility of intensifying economic friction.

In today's China, in the midst of growth, deflation is worsening. The government is raising salaries for public servants and has introduced more national holidays to stimulate consumption. How will all this affect the economy?

With an excess labor force of several hundred million people, how will China handle agricultural issues? How can China, a socialist state, improve its rudimentary social security system? Will a "national minimum" be implemented regardless of the consequences? Can China deal with the desire for private ownership of property unleashed by continued development of the market economy? Issues involving reform and enrichment of the social system are important and cannot be avoided.

Nishimuro gives a speech at an international symposium on "Chinese Economic Development: Implications for the Global Economy"

Where China's Economy is Headed

China's market economy has made rapid advances over the last 10 years. Since 2001, global FDI has fallen, but not in China. In fact, it increased in 2002, and also in 2003.

Increases in FDI have clearly contributed greatly to China's foreign trade. In the course of the 1990s, foreign trade increased fourfold, raising China's share of global trade. China's share of global exports increased from 1.9% in 1990 to 4.3% in 2001, while its share of imports rose from 1.5% to 3.8%. Foreign-owned companies account for a growing share of China's imports and exports, reflecting the build-up of production in the country. In 2001 they accounted for more than half of both imports and exports.

Economic theory tells us that a country tends to have a comparative advantage in the production of goods when the resources the country possesses in abundance are employed intensively. China with its huge workforce should have a comparative advantage in labor-intensive manufacturing. If Japan's export sector is to compete, it must invest in research and development (R&D) and raise productivity. That is the only way to overcome the comparative advantage of China's labor-intensive manufacturing. Recent research suggests that capital-intensive, advanced technology will remain in Japan. But does this economic theory provide an adequate explanation of foreign companies' inroads in China?

Many countries in Asia have comparative advantages in labor-intensive industry.

But why is China's performance so outstanding? This is because China's fast-growing economy includes colossal potential domestic demand, underpinned by a population of more than 1.2 billion, that is destined to come into its own in the future. In Shanghai and certain other cities the tempo of consumption has already quickened.

Another factor facilitating the shift of manufacturing to China is the establishment of infrastructure for manufacturing industry, such as export processing zones and industrial parks in special economic zones. Capital, technology and know-how from Taiwan and Hong Kong have flowed into southern China. Semiconductor and computer manufacturers from Taiwan have recently made inroads into China, accelerating the emergence of a Greater China. Products manufactured in Greater China will be exported to the United States and Japan. The economic sphere that will emerge encompassing Greater China, Japan, and the United States will become increasingly important in the future.

China's Role in the Development of the Global Economy

It is to be hoped that China will increase its share of world trade through the stable growth of its economy and make a great contribution to the global economy by accelerating the development of its domestic market.

As a result of China's accession to the WTO, the country has come under pressure from abroad to bring its financial and legal systems into conformity with international rules. Progress toward this will be monitored, under the accession agreement with the WTO. However, what is imperative is not to pursue overly strict monitoring, but to ensure systematic development that supports the attainment of stable growth. The stable development of China will have a beneficial impact on the development of the global economy. To this end, the United States, Japan and the ASEAN nations should discuss and exchange opinions on the direction of China, so that China can determine its own economic policy in the framework of the global economy.

Following the Asia-Pacific Economic Cooperation (APEC) Finance Ministers' Meeting in September 2003, the APEC Economic Leaders' Meeting was held in October. It is expected to discuss the exchange rate issue. I think it is important to address this issue from the viewpoint that it is a means of achieving a shared objective, that is, sound development of the global economy and the Chinese economy.

The WTO Ministerial Conference was held in Mexico in September 2003. Despite efforts to reach a consensus at the ministerial conference in Cancún under the Doha Development Agenda, the results were unsatisfactory. However, this does not mean the importance of the WTO has declined. There is no doubt about the critical role of the WTO in development of the global economy. In particular, China has a significant role to play as a leader of the developing countries.

China's economy is expected to become increasingly important as a driving force of the global economy. In order to ensure the future prosperity of China, we must put in place a framework that enables cooperation at all times. **JS**

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