China's Growth Slowdown

Why in news?

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The growth of gross domestic product (GDP) in the People's Republic of China (PRC) has slowed to 6.6% in 2018.

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Why is it a concern?

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- Fourth-quarter growth (year-on-year) was 6.4%, indicating that the economy was decelerating.
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- A $12 trillion economy growing at over 6% is still a powerhouse.
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- But by far the biggest contributor to global growth, the latest numbers are a cause for concern.
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- It is remarkably low for that country and is the lowest that GDP growth has been since as long ago as 1990.
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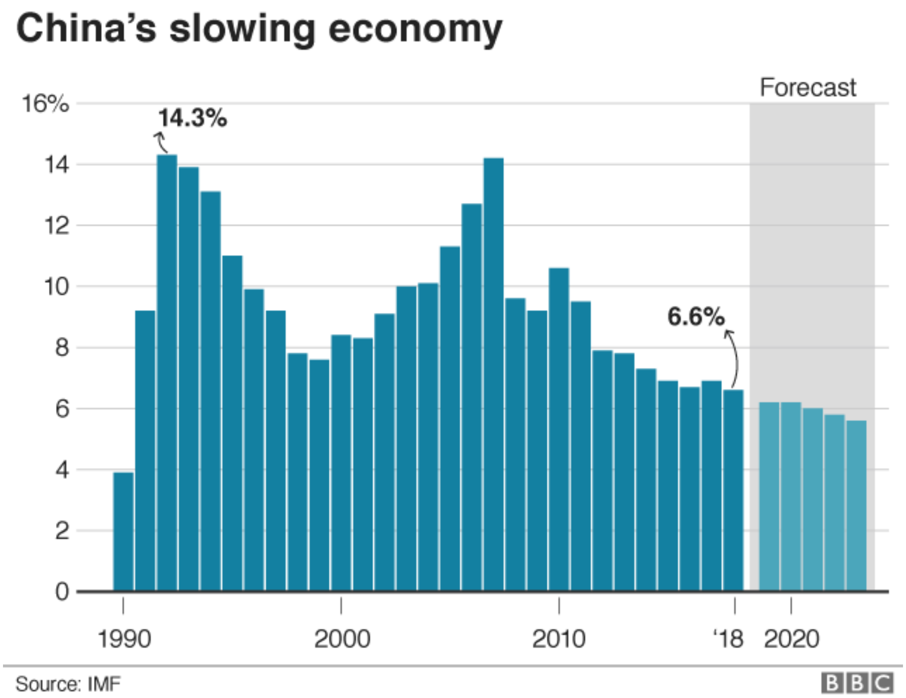

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What is the cause?

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- The growth slowdown is less cyclical and more structural.
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- Three decades of super-charged growth in mainland China was delivered by a very specific investment- and export-driven model.
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- Financial savings and foreign investment were routed to large, capital-intensive projects and export-focused manufacturing.
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- This allowed employment and incomes to grow significantly.
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- Eventually, the PRC became the world's factory, running large trade surpluses with most countries.
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- After the global financial crisis of 2008, the government made the choice to multiply on this model.
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- It took advantage of the cheap credit to various capital-intensive sectors.
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- But, while growth remained robust, the productivity of capital declined severely.
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- In the past year, three-fourths of growth has come from consumption.

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- This indicates that the consumption-focused sectors of the economy have now become the engines of progress, signalling an imbalance.

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What should China do now?

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- Beijing is well aware of the above structural problem.

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- There has been talk of “rebalancing” the economy away from exports and an investment obsession towards innovation and consumption.

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- To move from upper-middle income to high-income status (to avoid the “middle income trap”), China would have to raise productivity.

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- This has to come from moving up the value chain and embedding greater innovation in all its processes.

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What are the challenges therein?

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- The rebalancing process would naturally lower growth during the transition.

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- So implementing the changes is harder given the political pressures to ensure that growth remains high and incomes keep on rising.

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- Thus, the credit flow to unproductive sectors of the economy cannot be stopped entirely.

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- Furthermore, empowering the private sector, which is a necessary next step in the rebalancing, is contradictory to China's recent policy.

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- Also, with enough resources being spent on research, integrating the products thereon into final output has been much harder.

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- Given these challenges, the trade tensions with the U.S. may actually help in China's attempt to de-emphasise exports’ importance.

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What does this mean for India?

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- For India, the question is how much this structural slowdown will affect its own growth trajectory.
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- An opportunity has opened up to insert India further into global supply chains.
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- But, it is also essential to ensure that there are substantive domestic reforms to take advantage of the above.
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Source: Business Standard

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