

# **HOW WILL CHINA'S ECONOMY ADJUST TO LOWER GROWTH**

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## **Executive Summary**

1. China's high growth era—double-digit rates of growth for more than 3 decades—is drawing to a close. The recent World Bank study has also confirmed this.
2. No economy can keep on growing at such high rates without running into constraints and problems. The ending of such high growth is only a matter of time, and Chinese policy makers have come to accept this.
3. China's coming lower growth is very much in evidence by looking at its basic growth components on both the supply and demand side. Some key growth components will be gradually weakened over time as the economy itself is being restructured.
4. The end result is China's overall macroeconomic rebalancing, and its ensuing changes will in turn offer a good glimpse of how China's economy is adjusting to lower growth in future.
5. On the supply side, China's economic growth is driven by increases in the labour force and productivity growth or TFP (total factor productivity). For many years to come, China will still have to cope with the problem of labour surplus.
6. As China's labour problem due to ageing population will surface only towards the end of the 2020s, the major source of future growth will critically depend on TFP growth, which in turn depends on how China will come to cope with its innovation system and human capital formation.
7. On the demand side, economic growth stems from increases in both domestic demand (investment and consumption) and external demand (net exports). It has become crystal clear that exports will soon lose their comparative advantage and contribute much less to China's GDP growth.

8. China's future growth, to be sustainable, will therefore have to depend basically on domestic demand. Over time, the share for investment, currently the main driver of growth, will come down while the consumption share will correspondingly go up, as the growth strategy is increasingly skewed towards meeting *minsheng* (livelihood) needs.
9. Underlying China's existing unbalanced growth model based on over-investment, over-export and under-consumption is China's extremely high domestic saving rate (50% of GDP), which is set to come down after macroeconomic rebalancing.
10. All these will lead to the weakening of the basic sources of growth, and hence lower growth—the projected growth of 5% for the period of 2025-2030.
11. Still, by 2030, China's economy will have grown to be the world's largest, with a total GDP of US\$24.4 trillion (at current exchange rate), though its per capita GDP of US\$17,000 is about the level of Japan's in 1970 and Singapore's in 1993.
12. China will then be a developed economy, but it is still quite a distance from being an affluent society. So much for China's projected economic growth path 20 years down the road.
13. The political and social dimensions of the development process will be more intriguing, as more drastic political and social transformations will follow closely successful economic growth.