

**CHINA'S ECONOMY IN 2006/2007:
MANAGING HIGH GROWTH FOR
FASTER STRUCTURAL ADJUSTMENT**

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Executive Summary

China's economy in 2006 continued to chalk up high growth at 10.5%-10.7% with low inflation (CPI at 1.3%). For five years in a row since its accession to the WTO in 2001, China has sustained such growth momentum at double-digit rates.

China's "economic leadership" used to be deeply worried over possible "hard landing" from breakneck growth. But such fears had by 2006 largely dissipated. The prevailing national economic mood through 2006 had shifted from "fast growth" to "more balanced growth".

Basically, the so-called new development strategies (that were already incorporated into the 11th Five-Year Plan) were still built around high economic growth, which is deeply rooted in China's institutional structure.

Specifically for the sources of economic growth, China's high GDP growth in recent years has been primarily driven by investment. Fixed assets investment has been growing at 27% a year, compared to only 11% for consumption.

For a large economy as China, the contribution of external demand (or net exports of goods and services) to its GDP growth is relatively small, despite the post-WTO export boom.

What is now clear is that China today is already an important player of the global economy, operating as a source of regional and global economic growth and providing a catalytic effect for global economic integration—as China is the favourite home for many regional and global production networks.

China would not have become such a significant global economic participant had it not joined the WTO five years ago. In his recent assessment of China's WTO membership, Commerce Minister Bo Xilai proudly declared that China's post-WTO performance had "outpaced the expectations of not only foreigners but also ourselves".

The vindication of the WTO membership as a right policy plus China's record of having effectively managed its sustained high growth without a hard landing have greatly boosted the self-confidence of China's economic leadership.

China's economic elites are also fast learning the ropes of international economic diplomacy, particularly vis-à-vis other economic powers. Politically, militarily and technologically, China is far from being a great power. But as an economic aggregate, China has started its claim as an economic power (*jingji daguo*).

The outlook for 2007 is expected to be a moderate slowdown in growth to around 9.5%. But in the social and environmental areas, so many burning issues are crying out for the government's attention.

Faced with so many problems that require long-term solution, the government is characteristically resorting to its ideological weapon of building a "harmonious society". Basically, the people are asked to be more patient, letting further economic growth solve their problems.

Externally, China's record trade surplus (US\$160 billion) and its record foreign reserves (US\$1 trillion) – actually a manifestation of China's own serious external macroeconomic imbalances—will put the *Renminbi* and China's trade relations with developed countries under even stronger pressure.