

GENERAL DISCUSSION

China and the Global Economy

Mr. Prasad: You spoke really eloquently about why it is realistic to expect China to continue to grow at a high rate, and you also spoke about the challenges China faces that are recognized by the authorities and are part of the five-year plan. But what if those challenges are not met? Do you just see a slight slowing of growth or do you see a collapse of growth? What do you see as other big risks to China's growth?

Mr. Lin: Let me say that my prediction of 8 percent growth for China may be too conservative. China can tap into two sources of growth. One is the advantage of backwardness. The other is ongoing structural reform. If you put them together, the growth rate can be higher than 8 percent per year. I can be accused of being too optimistic about the future, but in reality I was too conservative in the past. In the book I published in 1994, I was one of the first to predict that China could continue to grow at an 8 percent rate for 30 years. I was accused then of being too optimistic because it has never been observed historically that a country could maintain an 8 percent growth rate for 30 years. In fact, in the past 32 years the average annual growth rate was 9.9 percent, primarily because of productivity gains from technology and structural reform.

Mr. Gourinchas: I enjoyed the picture you provided us with. It's very uplifting, especially in the current environment. At the same time, I want to come back to what Eswar was mentioning. When you think about the growth prospects for China in the next 20 years, the analogy you drew is to Japan, Taiwan, and Korea. As you mentioned, they were all following non-textbook growth strategies, relying on the external sector. The one big difference with China is its size, as you emphasized. To what extent do you think that strategy of relying on the external sector can be sustained? You mentioned some of the structural reforms. But if they're going to follow that strategy, which was outlined in the twelfth five-year plan, then we're off the path that was blazed by Japan, Taiwan, and Korea. Does that lead you to assess downward your estimates?

Mr. Lin: That's a good question. The East Asian economies took into account their comparative advantages when pursuing strategies to develop their economies. If a country follows its comparative advantage, it doesn't necessarily mean that it will have a larger trade surplus. It exports more and imports

more as well. In fact, the East Asian economies had some trade surplus, but not a large one, before 2000, even including China. The large trade surplus that emerged after 2000 was a new phenomenon, but it was not really related to the development strategies. There's also the transitional issue that a rapid-growing economy may have a trade surplus. Rapid growth will not necessarily turn into currency appreciation. I have some analysis in my book. I invite you to read it, and then we can debate.

Mr. Kim: My first question is related to the exchange rate. You mentioned that the high corporate saving rate and income inequality add to the saving rate, and this leads to external imbalances. Thus, the high saving rate in your domestic economy may mean that China will need to depend on external demand to achieve a certain amount of growth, which could result in an undervalued renminbi. But I wonder if the causality might run the other way around: Income inequality is caused by undervalued currency because you are exporting a lot and this tradable sector is generating a lot of income. As a result, income inequality follows the development strategy based on depreciated or undervalued currency.

Second, if China grows another two decades at 8 percent a year, it's probably the longest spell of over 8 percent for almost five decades, and you say this is a miracle. But I wonder if China is able to do this because of its population. Korea, Japan, and Taiwan initially grew very rapidly, but eventually they faced a lot of wage pressures in the labor market because they didn't have enough workers. China, because of its large population, can continue this kind of high growth for five or six decades.

Mr. Lin: Regarding causality, the large trade surplus in China did not appear until 2003. For many years before 2003, the trade balance was negative or balanced. And income disparity became larger and larger, but that didn't start in 2003. It started in 1986, following agricultural reform. This shows that this large trade surplus was not because of the income disparity in China.

Second, after 2003 China was not the only country whose trade surplus increased. Almost every country increased, including those countries competing with China in the export market—except for the U.S. [laughter]. And how could that be? Supposedly, undervaluation was the main reason China's trade surplus grew so large. Other countries competing with China should have had reduced trade surpluses. But in fact, they also increased. So I think the conventional explanation only looks at one side, one element. It's like the story of the blind man and the elephant. For the conventional explanation, it touches part of

the reality, but not the whole picture. And in the appendix of my book, I have a whole picture about the elephant [laughter].

Mr. Dekle: How can China start raising its consumption?

Mr. Lin: In fact, the growth rate of consumption in China is not low, it's very high, although it's less than the growth rate of investment. I can give you my personal story. I was the first one in my generation to get a PhD in social sciences and return to China in 1987. At that time, not many people returned. So the Chinese government had a very attractive policy to encourage people like me to return. That is, I could bring back a car without paying custom duty [laughter]. And the custom duty at that time was 215 percent. Certainly, I'm a rational person, trained in Chicago, so I brought a car back to China. It took almost 10 months for me to get a license, so then in April 1988, I could drive my car on the street. When I went to get my license, the transportation authority told me that my car was the second privately owned car in the whole city of Beijing. Can you imagine how many privately owned cars there are in Beijing now? More than three million. So actually, consumption in China also increased very rapidly.