Why has China grown so fast for so long?

Prospects for the future

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Context

- China has become a different country in just three decades
- Traditional economic theory is insufficient to explain this stellar growth and development
- ‘Development as transformation’ perspective key to understanding China’s success
- What are the implications for China’s future growth, and are there lessons for other developing countries?
China’s development results

• Largest sustained GDP growth ever witnessed, outperforming the previous “Tigers”: over 9 percent annually in per capita GDP.

• Share of world trade tripled since 1990 and still rising fast

• Reaching per capita GDP of over $2000 means China is no longer a low income country

• Alone responsible for the absolute reduction of global poverty

• Not merely economic: HDI .75 in 2003 (up 43% from 1975)
...exceeding other “Tigers”

GDP per capita, China vs. India and ASEAN-4 (1980=100)

Source: IMF (2007)
Growth yielded massive poverty reduction

- Official poverty fell from 15% in 1984 to 2% in 2006
- $1/day poverty fell by 500 million in 1981-2008
- Excl. China, global poverty actually increased by 29 million
- Regardless of measure used, the most dramatic poverty reduction in known history

**Official and $1/day poverty headcount (%)**

Source: UN and LGOP

![Graph showing poverty reduction over time](image-url)
As a result, China is regaining its place

China’s share of world GDP, selected years 1500-2003 (%)

Source: Maddison (2006)
Economists struggle to understand

- Neoclassical studies see growth and development as a ‘simple’ problem of accumulating and allocating factors of production.
- The resulting emphasis is on rapidly creating ‘standard’ policies and institutions regardless of country-specific context.
- Privatization, liberalization and market pricing are seen as key for accelerating growth.
- But China did not follow any of the standard prescriptions in the so called Washington Consensus.
- And yet the Chinese bumblebee continues to defy the laws of neoclassical gravity.
- Is this the beginning of a Beijing Consensus?
The role of Capacities

**Individual capacity**
- Human development achievements provided the foundation
- Gave capability to respond to new incentives and opportunities
- HD-growth linkages have been empirically established

**Institutional capacity**
- Early institutional transformation underpinned economic reform
- Capacity upgrading has been a continuous priority
- Strong results orientation and link to career development
- Government a supportive agent more than an obstructive one
- Large public inv. to open markets (incl. infrastructure)
1. Investing in human development

Average Schooling Years of China’s Population Aged Between 15-64 for the Period 1952-1999

Deng saw need to revitalize the bureaucracy as first step in reform

Produced distinct change in officials age (top), tenure and educational level (bottom)

Resulted in both higher capacity and better alignment with reform

Younger, better educated cadres more supportive of reform process: building constituencies for change
3..Social capital and cohesion

Social capital:

- Strong cohesion thanks to homogeneity and historic equality
- Informal institutions counter market/institutional failures (viz. informal finance, guanxi, “friends first, business later”)
- Trust systems offset absence of formal contract enforcement
- Mindsets ready for change after previous system found lacking
- Faith in central government and buy-in on new path forthcoming

The above made society responsive to reform and new incentives Far outweighed market imperfections in promoting rapid growth
The role of **Policies**

- Policies did not conform to standard western paradigm, but were in alignment with the context and capacities
- Sequencing policy vs. institutional reform needs further study
- But detailed policies seem initially of secondary importance as the more fundamental transformation mattered more
- As the institutional framework is refined, getting policies right is now of increasing importance
- Capacities must also be aligned to respond to the new policies
...partly thanks to lower population growth

Population growth (%)

Source: Penn World Tables (2005)
However there are also challenges

- Substantial rise in income and non-income inequality
- Rural population increasingly elderly, female and vulnerable
- Rural-urban and other gaps are reducing social cohesion
- Migrant workers unprotected in the cities they build
- Ageing population creating steep future pensions challenge
- Signs that the poorest no longer take part in growth

P.c. income urban/rural residents, 1990-2003
Source: UNDP
The poor may even be sliding backwards

Per capita income growth by decile, 2001-03; preliminary analysis

The fiscal burden is heavy on local levels

- Fiscal mechanisms, decentralisation once stimulated incentives, now limit equal access to public services
- Local government increasingly burdened by unfunded mandates
- Fiscal pressures spawn unwanted tactics in search of revenue
- Local government legitimacy weakened, increasingly seen as hindering balanced development

Fiscal revenue and expenditure p.c. (yuan)
Much potential for growth remains...

- High growth will continue, for several reasons:
  - Many inefficiencies remain to be addressed
  - New institutions further adapted to the needs of the current phase will deliver better results
  - Unification of the rural and urban economies will bring many benefits of scale and efficiency for a time to come
- Structurally, increasing marketization is making traditional economic factors and institutions more important
- Given the strong economic fundamentals that have evolved, if realignment succeeds this may only be the beginning
...if the transformation continues

- As China develops the next stage of reforms, some features key to previous success should be revisited
- Policies have already moved in the right direction (Xiaokang, the five balances, New Socialist Countryside)
- The challenge is how to effectively implement them
- China too large & complex to manage easily, so strengthening rule of law and scientific development is now key
- The Chinese reforms show the importance of alternative approaches to development, beyond Washington consensus
- Towards a Beijing consensus?
Will China keep on growing?

- Holz (2005): By 2010 (in PPP)
- Keidel (2008): By 2030
- Fogel (2006): By 2030
Potential lessons for other countries

- Ownership at all levels of society cannot be overemphasized
- Public policy is vital in creating the individual and social capacities to generate and sustain reform and growth
- Perfect classical policies and institutions not immediately necessary: home-grown solutions may work better
- Encouraging grassroots unorthodoxy and scaling up initiatives that work is better than top-down formulaic programming
- Long-term commitment to reform and development by leaders and ruling class is critical
- Building constituencies for reform and paying off losers reduces social disruption, ensures sustained progress
- Per capita improvements require managing population growth
Thank you