Global downturn threatens Chinese economic growth

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One of the major questions on the agenda of China's National Peoples Congress (NPC), which meets this week, will be the impact of the downturn in the world economy.

Some sections of the Beijing regime are predicting that, despite the international situation, China is on the eve of a massive economic expansion due its entry into the World Trade Organisation (WTO) last December and the hosting of the 2008 Olympic Games. China's chief negotiator at the WTO talks, Long Yongtu, forecast last November that, within 10 years, 400 to 500 million Chinese would enjoy a "middle-income" life, making China a "much bigger market" than the United States. Similar claims are being made as part of Olympic investment promotions. According to a recent forecast by the Chinese Academy of Social Sciences (CASS), China will have a 200 million-strong middle class, able to "buy cars and housing and spend money on leisure travel" by 2005.

The conviction that the growth of the middle class will drive the next stage of China's economic development underpins the forecast by the Chinese government that the country's Gross Domestic Product (GDP) will grow by 7 percent this year. The head of the central economic authority, Zeng Peiyan, declared the growth figure achievable due to "the huge potential of [China's] market and people, the increasing competitiveness of its enterprises and human resources, high savings rate and abundant foreign reserves".

However, the driving force of China's economic expansion in the 1990s—during which the regime claims GDP grew by an average of 9.2 percent annually—was not domestic demand from a burgeoning middle class, but high rates of foreign direct investment (FDI). Ten years ago, South East Asia attracted half the Foreign Direct Investment (FDI) in Asia outside Japan, with only 20 percent flowing to China. From 1996 to 2000, this proportion reversed, with the annual average FDI to China reaching $US42.7 billion, or 80 percent of the FDI in Asia outside of Japan.

The Ministry of Foreign Trade and Economic Cooperation announced on January 14 that FDI in 2001 grew more than 10 percent. Last year, a total of 26,139 foreign-invested firms were set up in China, with a total contracted FDI of $US69.191 billion. The total number of foreign companies in China has reached 390,000, with contracted investment standing at US$746.9 billion.

The foreign investment has flowed primarily into export industries. China provides companies with a low-cost, regimented workforce and special economic zones offering convenient ports, low land costs and negligible taxes. Of the 845 export processing zones in the world in 1997, employing 27 million workers, more than 60 percent were located in China. The foreign investment is concentrated in the south and eastern coastal regions such as Shanghai, Tianjin, Beijing and the Pearl River Delta opposite Hong Kong. China's export zones now produce one third of the world's labour-intensive products. The free trade zone of Shenzhen, in the Pearl River province of Guangdong, produces half the world's watches.

China's low production costs have become an essential ingredient in the efforts by transnational corporations to maintain their profitability under conditions of intense competition. General Electric, for example, supplied one third of its global sales last year from Chinese contractors. China is now the seventh largest trading nation, with $249 billion in exports and $225 billion in imports. Exports and foreign investment generate 40 percent of GDP.

The onset of recession internationally therefore is putting immense strains on China. The most recent statistics point to an accelerating slowdown. Figures released last week put the annualised growth in the last quarter of 2001 at just 6.7 percent, slowing from 8.1 percent in the first quarter, 7.7 percent in the second, and 7 percent in the third. The main factor in the slowdown was falling export growth. Last year, exports increased by only 7.3 percent, compared with a 27 percent growth in 2000.

One State Development Planning Commission economist, Wang Jian, doubts a 7 percent growth this year. He told the *South China Morning Post*: "Last year's decline in export growth was caused by the worsening global economic situation. This year, world economic expectations are even lower and that resulted in my downbeat judgement."

China's exports are also coming under added pressure due to the recent devaluation of the Japanese yen. According to a study by finance house Morgan Stanley, if the yen devalues 10 percent, the GDP of the rest of East Asia will fall by 1.3 percent due to the loss of markets to Japanese competitors.

In Guangdong province, China's key export region, the slowdown of export growth is already impacting. Bu Xinmin, the director-general of the Guangdong Statistics Bureau told *Hong Kong iMail* on January 17 that the province's growth in 2002 would drop to around 8.5 percent, compared to 9.5 percent last year and 13.6 percent in 2000. As a result of the slowdown, he also admitted unemployment was the "highest since the early 1980s".

Consumer demand from within China will not be capable of offsetting falling export demand. While there has been the growth of a middle class, it is not large numerically and its fortunes are largely bound up with foreign trade. A study released in March by the State Statistical Bureau found that less than three percent of the urban population—some 12 million people—had a household income of $US60,000 or more. While they can afford cars, computers, TVs and other consumer items, they are a small market. China's domestic auto sales are comparable with Belgium's, a country with a population of just 10 million. Only 10 percent of the urban population earn more than $US3,600 a year. The average is just $760.

An economic adviser for the Bank of China told the February 12 *South China Morning Post*: "To become a low-cost production base for the world is China's only option, but it is very dangerous choice... Your technology, capital and market come from abroad, only production is at home. This model is very weak and cannot resist attack."

While the export sector has boomed since the mid-1990s, most of the domestic economy has been mired in stagnation and overcapacity. Thousands of previously state-owned companies have been closed down in the last five years in order to eliminate excess or inefficient production, but the crisis continues.

The latest national survey of 600 major products by the State Economic and Trade Commission, released in December, indicates that only 82 will experience a balance of supply and demand, while 518 are in oversupply. Overproduction and inventory growth is predicted to rise another 3.4 percent this year. The overcapacity has fueled deflationary tendencies, marked by falling prices. The Consumer Price Index fell one percent in January—the sharpest fall in two years.

According to the Chinese Economic Information website last December, products in oversupply include "home appliances, cottons and agricultural and industrial producing materials, as well as the low-end food products, such as fruits, liquors and sugar."

A vast pool of unemployed labour exists that the export industries cannot absorb. According to the latest statistics from the Labour and Social Security Ministry, official registered urban unemployment reached 6.81 million at the end of last year. This figure did not include 5.15 million laid-off workers from state-owned enterprises who have not found other jobs and the officially admitted 120 million "surplus" workers in rural China who cannot find steady employment either in farming or in regional industries and businesses.

Now, unemployment is set to soar with China's entry into the WTO. More competitive foreign producers—particularly in agriculture—will also be able to import more freely into China due to the reduction of tariffs. Imported foodstuffs are expected to drive up to 20 million farmers off the land. Chinese subsidiaries of major transnationals will also be able to compete directly against local producers in such areas as banking, insurance, telecommunications and petrochemical industries. Although some jobs will be created, many more will be lost in the bankruptcy or buy-outs of Chinese companies.

Unlike the optimists, the more sober sections of the Chinese regime are becoming anxious over the stability of its rule. A campaign was launched for the Chinese New Year for government departments to "show compassion" toward the poor and 18 new White Papers have been issued stressing the extent of poverty. Behind the sensitivity to social inequality is the animosity between the majority of the population and the small number who benefit from the government's free market economic agenda. Social discontent is swelling in both rural and urban areas. An official report last year admitted to 30,000 protests involving a large number of people—an average of 80 per day.