Goals for the Course

- To understand and contextualize China’s development strategy since 1978
- To gain insight into economic outcomes available to China in the near future
- To understand the potential impact of the coming crisis in China on the Americas
- To improve our understanding of what sort of economic relationship with China Mexico would find useful

Course Outline

1. China's Development Strategy Post-Mao: the Theory
2. The Reality
3. Where the Plan Went Wrong
4. Urbanization, Debt, and the Banking System
5. Industry Focus: Agriculture and IT
6. The Stimulus Program 2008-2011
7. The Wealth Market, the Banks, and China's Local Politics
8. Catalysts for Crisis
9. Lines Across the World: China's International Links
10. The Aftermath

China’s Post-Mao Strategy

- “Cheap Labor, Cheap Capital, Cheap IP”
- Repressing Consumption
- Increasing Debt

Amassing Capital

Background: The payments crisis and Deng's plan to obtain hard currency

- Trade policy adds to savings
  - Import quotas, high tariffs
  - Special zone system: blamed on a need for cultural isolation, actually the zones created a bureaucratic cut-out enabling entrepreneurial officials to capture tax revenues to match the investment they brought in
  - Huge infrastructure investment in the zones to support exports
- Attracting FDI
- Repressing Consumption
  - Wage growth lags productivity growth
  - Migrants to cities get a productivity boost from mechanization. Hukou system keeps migrants from participating in city life. Unions are prohibited. Social safety net has eroded, creating a subsidy for trade.
- Undervaluing the Currency

Trade Policy Measures

- Import quotas, high tariffs
- Special zone system: blamed on a need for cultural isolation, actually the zones created a bureaucratic cut-out enabling entrepreneurial officials to capture tax revenues to match the investment they brought in
- Huge infrastructure investment in the zones to support exports

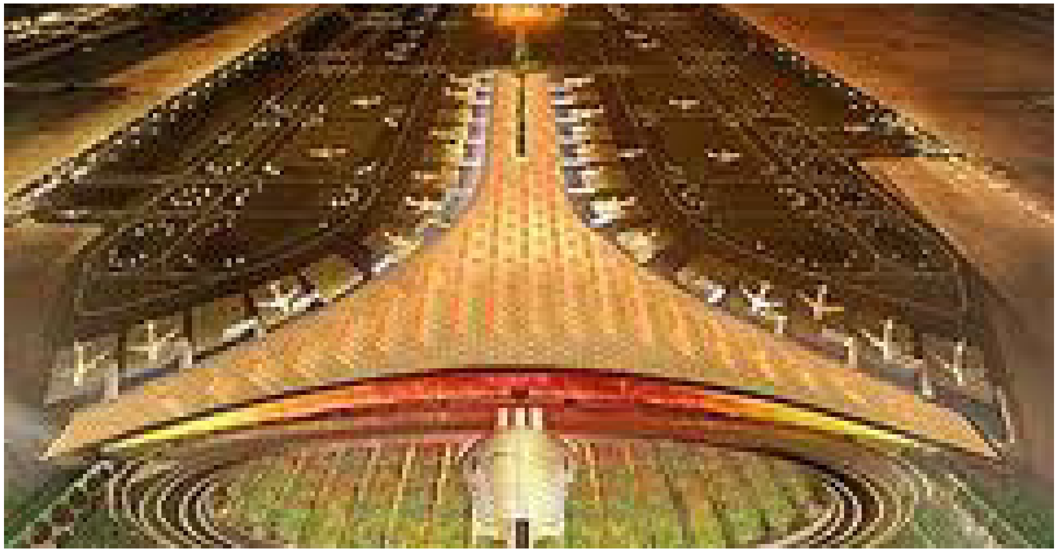
Focus on Export Earnings:
The old treaty ports, the new Open Zones

Foreign Direct Investment Measures

- Red Carpet Treatment
- Focus on tech transfer
- Policies promoting promulgation of technology through industrial ministries
- Programs to attract “returnees” with start-up capital provided they carry in needed technologies
- Funding programs designed to replicate successful overseas technologies

Pleasing Foreign Investors

- The top-priority infrastructure for Beijing in the 1980s as its airport road, then mostly unused.
- Every iteration of the Capital Airport has been more monumental in scope and imposing in visual design.
- Foreigners used to be restricted to 3-5 star hotels, and hotels were awarded stars largely based on the impressiveness of their lobbies.



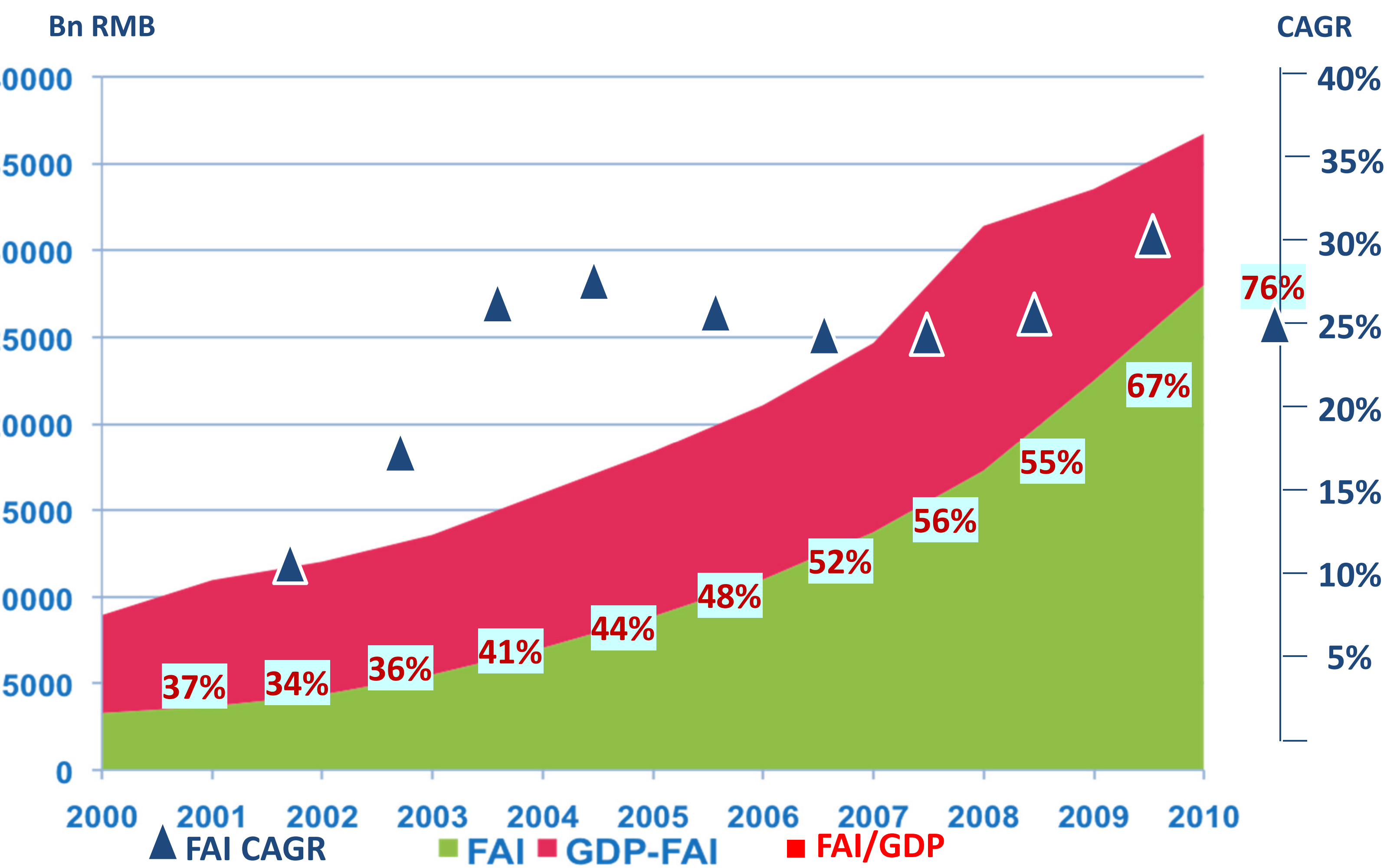
Repressing Consumption

- Investment as a share of GDP rises from under 25% (1990) to over 50% (2011)
- Household income drops from 72% of GDP (1990) to under 50% of

Under-valuing the Currency

- Post 1994: Peg to US dollar creates a form of consumption tax on imports
- Exporters receive a “subsidy” in the form of currency

Increasingly dependence on fixed asset investment

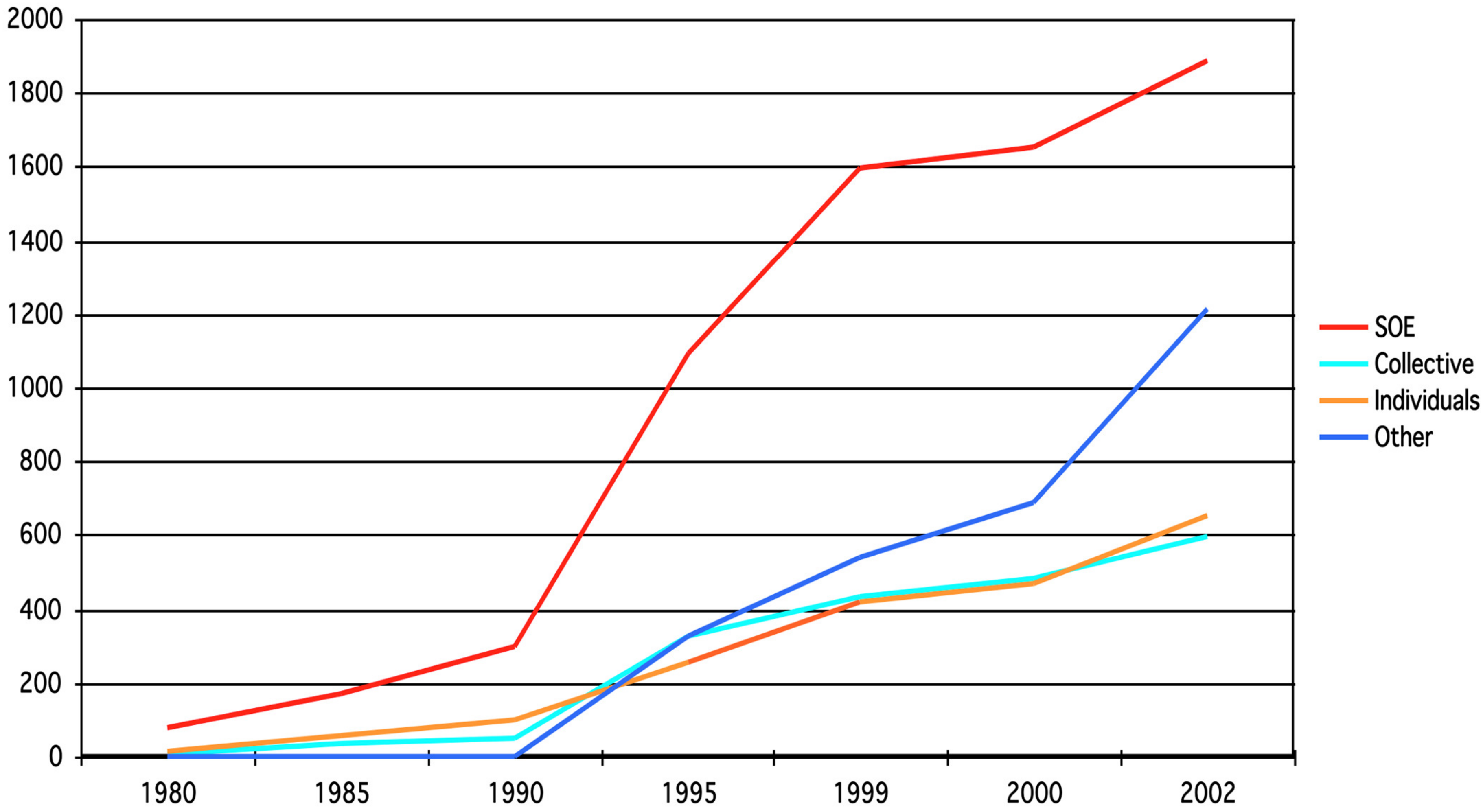


Every year, China needs more investment in fixed assets in order to generate roughly the same level of top-line GDP growth.

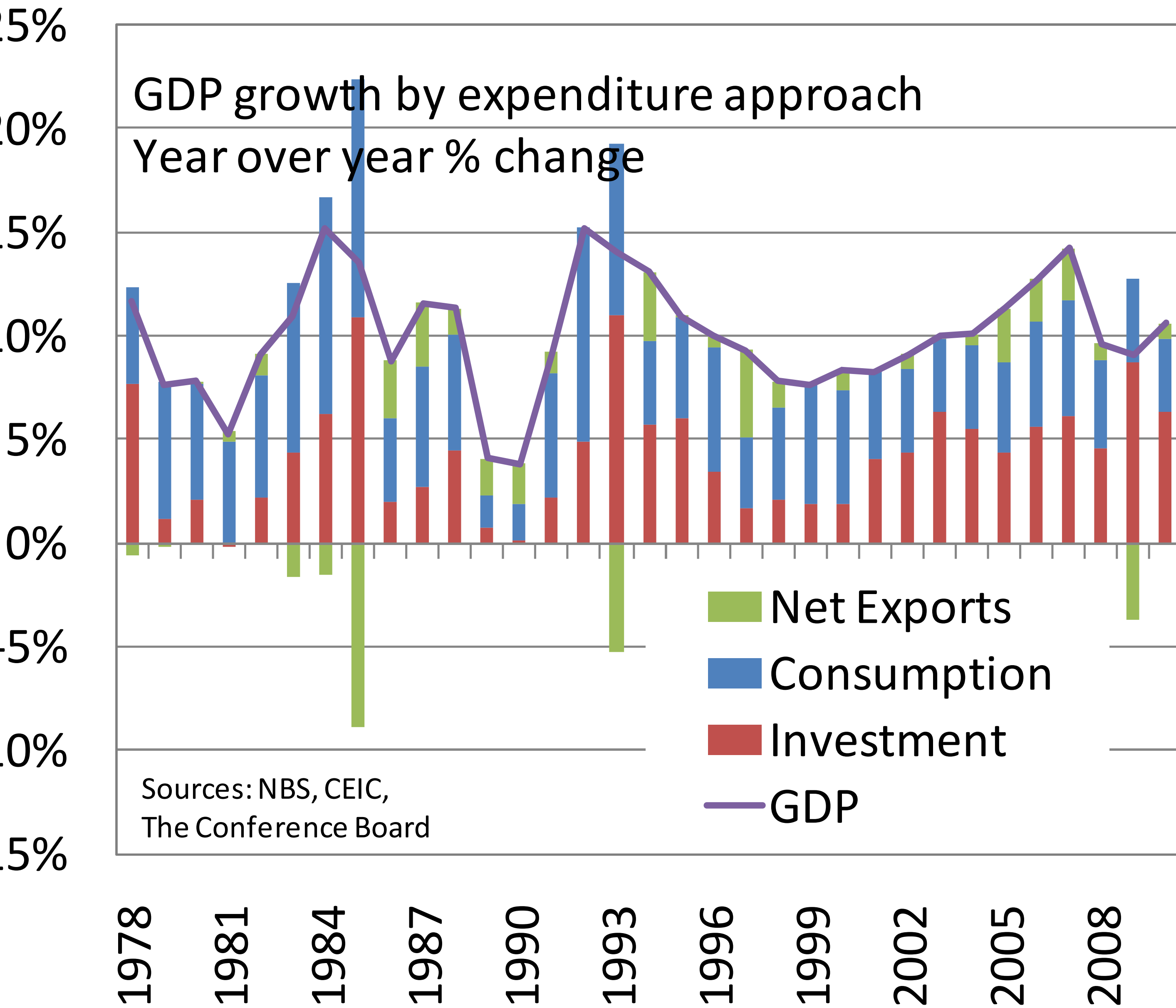
Increasing Debt

- In the early years, diversion of capital into infrastructure was efficient. It gradually become less efficient. Why continue?
  - Capital investment enables rent-seeking behavior
  - Creates momentum that is politically attractive—the perception of progress, employment growth
  - The newly “privatized” governing elites have a stake in the property and plant that is being subsidized
- As the investment becomes less efficient, it has to rise to maintain the same level of growth. The nation begins borrowing.

More Concentrated Investment in the State



Investment as the primary growth driver



- The Chinese government has used its political power to centralize national wealth and spend it on generating shor term growth.
- In the early post-Maoist years, this approach was very successful. Since the late 1990s, it has been less successful a generating wealth and welfare for Chinese people, more successful at sustaining the capital-infrastructure boom.
- Spending is an ever-more-costly way to generate growth and probably undermines long-term corporate investment in the finance, technology, services, and so on that would support long-term wealth.

Deploying Capital

- Export-oriented industries
- Ever more capital-intensive programs
- Real estate development
- More expenditure by government

Comparison: Brazil ~1965-75

Brazil’s Strategy

- High income taxes
- Massive investment in infrastructure
- State ownership of 75% of the economy
- Labor migration to coastal exporting zones
- Reduction in the proportion of rural labor

- The capital-accumulation strategy is not uniquely Chinese. Japan, Korea, Malaysia, Brazil, and may other countries have used many of the same strategies.
- For centralized, authoritarian governments, the strategy can be extremely successful for a time.

Discussion Questions

- What is a “socialist market economy,” and does it have specifically Chinese characteristics?

- What are some of the benefits the strategy has conveyed to the Chinese people and the Chinese economy?

- What are some effects China’s development strategy has had on the rest of the world? For example, with respect to:
    - Currency?
    - Tech transfer?
    - As an economic model for others?