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Session 40

Dialogues on Chinese Economy

Looking at the Economy from the Supply Side

Time: 13:35 - 15:00, March 26, 2017

Venue: ICC, Level 1, Dong Yu Grand Ballroom D

Moderator: WU Bofan, Host, Dong-Wu Talk-show

Panelists:

Robert KOOPMAN, Chief Economist, WTO

David Daokui LI, Dean, Schwarzman College, Tsinghua University

Justin LIN Yifu, Professor and Honorary Dean, National School of
Development, Peking University

LONG Yongtu, Former Vice Minister, MOFTEC

Key points:

➤ The supply problem has become a main aspect of conflict at the present stage of China's economic development.

- Against the backdrop of rapid increase of medium and high-income people, the main purpose of supply-side reform is to meet people's increasing consumption demand. The supply-side structural reform, by nature, is “kidney reinforcing” for China's economy, that is, enhancing vitality, increasing investment, and exploring new market.
- “Innovation” is the keyword behind supply-side reform. China should emancipate thoughts, and seek institutional breakthroughs.
- The primary challenge confronting China's supply-side reform is not what products China can provide for consumers but the improvement of supply efficiency.
- Supply-side reform and industrial policies should be complementary, and supply-side adjustment and industrial policy support should coordinate with each other.

Synopsis:

The supply problem has become a main aspect of conflict at the present stage of China's economic development. Currently, Chinese market is facing inadequate effective supply and excessive ineffective supply. As a result, the increasing consumption demands cannot be satisfied. The three major driving forces of economic growth, namely investment, consumption and export, are inadequate to drive the further development of Chinese economy. Since the proposal of supply-side structural reform, all walks of life in China, from governments to non-governmental organizations and from academic circles to media have

joined the discussions. What problems have emerged in the supply side of Chinese economy and how to conduct the supply-side structural reform have become topics drawing extensive attention and discussions from all walks of life.

The Supply Problem Has Become a Main Conflict in Chinese Economy

LONG Yongtu noted that the supply problem has become a main aspect of conflict at the present stage of China's economic development. Over a very long period in the past, China has been trying to increase export by "tightening belts", with import serving export in order to promote the development of processing trade in China. In the early period of reform and opening-up, as a multi-layered global market had a large amount of demands for Chinese products with low price and high quality, China's export has been developing very smoothly. Through three decades' development, the number of people with medium and high income has been increasing rapidly, and a huge number of middle-class people have emerged. Families whose per capita annual income reach RMB 60,000 to RMB 220,000 account for 65% of the total, hence the large-scale, high-level and high-quality consumption demands. As a result, a large number of Chinese consumers go abroad to buy imported products. The supply-side conflict has become prominent.

Robert KOOPMAN noted that there is a historical reason for proposing supply-side reform. In the past, China's production supply side mainly met its exports,

and particularly in the early period of reform and opening-up, China won the international market mainly by relying on export. Today, China's supply-side reform is a transitional course for meeting domestic demands, the re-allocation of China's domestic resources, and the transition of economic actions towards service industry. But it is more the generation of self-sufficient consumption.

David Daokui LI noted that the purpose of the supply-side reform is to enhance economic vitality. Over the past 40 years, supply-side reform has always been a magic key to economic reform in China, including the supply-side reform of rural household contract responsibility system, the price reform in 1985, and the state-owned enterprise reform in 1999, among others. If the economic reform in China for stimulating total demands around the 2008 Financial Crisis resembled "appetizing" in traditional Chinese medicine, then today's supply-side structural reform is similar to "kidney reinforcing", namely enhancing vitality, increasing investment, and developing new market.

David Daokui LI also stressed that China's supply-side structural reform differs from the supply-side reform in the west, as "the supply in China is not the same as in the West". The supply-side reform in the West is embodied in such measures as state-owned enterprise privatization, control reduction and tax reduction, while China's requirements on state-owned enterprise reform are to "become larger, stronger and better", so as to promote the reform guidelines of "delegating power, streamlining administrations and optimizing government services", while implementing structural tax reduction.

WU Bofan noted that the strong stimulation of consumption desires by “appetizing” superficially can drive economic growth, but the actual internal problems are not resolved. The lack of marketable supply is a fundamental reason for the failure to satisfy demands.

Import or Export?

Justin LIN Yifu noted that in 2016 China’s imported manufacturing products amounted to USD 1.2 trillion. It is because some products cannot be produced domestically that China has chosen to import them. In the field of tourism consumption, the value of high-end commodities purchased overseas by Chinese tourists has exceeded USD 100 billion, which is sufficient to reflect the gap between domestic effective supply and demand.

WU Bofan noted that China’s mainly imported production materials instead of consumption materials. China imported raw materials and production tools to produce products, which were then sold worldwide, and based on this model, China’s conducted export processing trade. However, great changes have taken place in the current market environment and development objectives, as people have started to desire more living materials to enter China. In terms of export, many Chinese equipment-manufacturing industries are very strong in the world. While import grows, export growth is also robust. Therefore, the structure of China’s import and export has changed..

Justin LIN Yifu stressed that in the globalization system, trade will inevitably and always involve both import and export. No country can manage to have only export while importing nothing. Economy is an ever-transforming and upgrading process. When dealing with the structural changes of import and export, we should distinguish between cyclic phenomenon and long-term development trend. From the perspective of long-term economic development, constant industrial upgrading and technological improvement and innovation are eternal topics. An analysis from the cyclic perspective will find that the global economy has not recovered from the 2008 Financial Crisis, with sluggish demands. The economic growth rate in China has dropped from an average annual rate of 10% to the current “new normal”. Many countries including the United States and South Korea face the problem of overcapacity. China should find differentiated and corresponding solutions on the basis of comprehensive analysis.

Robert KOOPMAN noted that in international trade, a country’s comparative advantages will not be maintained for a long time, and they will keep changing with the global market environment and national development. China should keep upgrading and developing its own comparative advantages and all aspects of the society should make good preparations and take an active part in the changes.

Innovation is the Keyword Behind Supply-side Reform

Robert KOOPMAN noted that supply-side reform should resolve not only the problem of what to produce but also how to produce more efficiently. The primary challenge confronting China's supply-side reform is not what products China can provide for consumers but the improvement of supply efficiency. What we should consider in the course of reform in China is whether to aim at becoming "bigger" or becoming "richer". For China, it is not important whether it will become the largest economy in the world. What matters more is whether its people can become richer.

LONG Yongtu noted that China is in a period of economic transformation. In the past, China has been simply pursuing economic growth speed, while now it is trying to improve quality. The main purpose of supply-side reform is to meet people's higher consumption demands, make them enjoy cleaner water, fresher air, and more livable cities, instead of just to improve GDP aggregates. How to produce products of higher quality more efficiently is one of the key points of supply-side reform. As a result, China gives priority to "innovation" in the five major ideas of development.

WU Bofan noted that innovation is the keyword behind supply-side structural reform. China's current supply system is seriously backward, and institutional supply has increasingly become a force of constraint and restraint. Today, the keywords for supply-side reform are reform and innovation.

David Daokui LI noted that China's young people and enterprises have plenty of innovation but, and in fact it is the lack of innovation in government that has constrained the development of Chinese economy. In today's supply-side reform, we should emancipate our thoughts, seek institutional breakthroughs and further drive the innovations in technical and commercial models. We should summarize our experience in the reform of the past 40 years, bring into play the initiative of local governments, cultivate market from the roots, manage well enterprise reform, give full play to the creativity of market, and let the two hands of government force and market force make efforts towards the same direction. This is the essence of the supply-side structural reform.

Justin LIN Yifu noted that supply-side reform and industrial policies should be complementary, neither of which should be over-stressed or neglected. Supply-side adjustment is an inevitable result from constant improvement of labor productivity. The improvement of the production level inevitably relies upon constant innovation of industrial technologies. With constant emergence of industries with higher added value, if there is no supply-side adjustment, then no development will be achieved in labor level and income level. On the other hand, as China is a country in transition and takes a progressive path, its development and transformation are going on at the same time. Over thirty-plus years of reform and opening-up, China has maintained economic growth, thanks to the constant adjustment and reform on the supply side. But many measures in fact fall into the

category of industrial policies. Without the support of industrial policies, it will be very difficult to have a good institutional environment for technological innovation, industrial upgrading and basic research.

LONG Yongtu noted that Chinese economy indeed needs the support of industrial policies, but all enterprises should be treated equally when such policies are implemented. If industrial policies did not apply to all enterprises, it would be difficult to produce truly competitive enterprises.