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CHINA’S ECONOMIC RESTRUCTURING AND THE BELT AND ROAD

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Characteristics and process of China’s economic restructuring

In the initial stage of reform and opening up, China’s economic restructuring mainly refers to the transition of economic system, i.e. the transition from the planned economy to the socialist market economy. In 1995, the CPC Central Committee officially employed the phrase “change the pattern of economic growth” for the first time in the Party’s document and proposed to “implement two fundamental changes”. According to the document, while transforming the economic system, we should promote the transition from an extensive pattern of economic growth to the intensive one, and China’s economic restructuring began to exhibit the characteristics of “double transition”, namely, institutional transition and development transition.

As the first five-year plan under the conditions of the socialist market economy, the 9th Five-Year Plan (1996–2000) explicitly proposed to implement “two fundamental changes that have holistic significance”. However, following the outbreak of the Asian financial crisis in 1997, China adopted some policy measures to cope with the crisis, such as expanding domestic demands, issuing government bonds, increasing investments in infrastructure such as highways, water conservancy and cities, expanding the scale of enrolment in higher education, and accelerating the reform of housing marketisation. As a result, the pattern of economic growth did not change substantially during the 9th Five-Year Plan period.

The 10th Five-Year Plan (2001–2005) pointed out that “China’s economy had already reached the point where we could not further develop the economy without making structural adjustments. Under the old economic structure and its crude manner of growth, products would not be marketable, and it would be impossible to sustain resources and preserve the environment.” The plan also proposed to make a proactive and all-round strategic adjustment of economic structure and combine the adjustment of the patterns of economic development between different industries, between different regions, and between urban and rural areas, with emphasis on the industrial structure. With China’s accession to the WTO in 2001, the Chinese economy once again entered a double-digit rapid growth period driven by foreign trade. However, under the export- and investment-led development pattern, the imbalance between internal and external demand structure and investment and consumption structure has further intensified.
The 11th Five-Year Plan (2006–2010) stated that China’s “rapid development had caused some serious problems: uncoordinated relationship between investment and consumption, blind expansion of some industries, overcapacity, slow transition of the mode of economic growth, excessive energy and resource consumption and worsening environmental pollution”. The plan called for propelling three transitions in the mode of economic growth: the transition from relying mainly on investment and export to relying on a well-coordinated combination of consumption, investment, domestic demand, and foreign demand, the transition from mainly relying on industries and quantity expansion to primary, secondary, and tertiary industries jointly driving economic growth and optimisation and upgrading of industrial structure, and the transition from relying heavily on increase in input of resources to relying mainly on improvement in resource utilisation efficiency. In 2007, the report to the 17th CPC National Congress changed “the transition of economic growth mode” to “the transition of economic development mode” and explicitly specified the new requirements for “accelerating the transition of economic development mode”.

During the 11th Five-Year Plan period, China’s economy grew at an average annual rate of 11.3%, and China overtook the United Kingdom to become the world’s fourth largest economy in 2006, overtook Germany to become the world’s third largest economy in 2007, and overtook Japan to become the world’s second largest economy in 2009. In 2010, China overtook the United States to become the world’s largest manufacturer. China has achieved in several decades what took developed countries centuries to achieve and created a miracle in global economic development. However, China’s economic transition failed to achieve the desired results under the influence of the global financial crisis in 2008. China’s launch of a large-scale bail-out plan on the one hand has prevented drastic economic downturn, but on the other hand it has also caused negative effects such as excessive production capacity and inventory and high leverage ratios.

During the 12th Five-Year Plan period (2011–2015), China’s economy showed an L-shaped development trend under the influence of structural factors at home and abroad. The growth rate had been declining year by year since 2011, falling below the record low set in 1991. In this regard, Xi Jinping has made a judgement that a significant characteristic of China’s economic development is that it has entered a state of “new normal” and clearly pointed out that:

the economy should shift gear from the previous high speed to a medium-to-high speed growth, from an extensive mode that emphasized scale and speed to a more intensive one emphasizing quality and efficiency; the economic structure is shifting from increment-and-capacity expansion to one with simultaneous stock adjustment and increment optimization; the new driver for the economy is shifting from being driven by input of factors such as resource and low-cost labor to being driven by innovation.

Xi Jinping also stressed that “a new normal period is a stage that China must endure if it is to upgrade and optimize its economy”, which points out the direction for the deepening of China’s economic restructuring.

The path and effectiveness of China’s economic restructuring

The report to the 19th CPC National Congress held in 2017 stated that “China’s economy has been transitioning from a phase of rapid growth to a stage of high-quality development. This is a pivotal stage for transforming our growth model, improving our economic structure, and
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fostering new drivers of growth”. The report also proposed the path for transitioning economic development. That is, “We should pursue supply-side structural reform as our main task, and work hard for better quality, higher efficiency, and more robust drivers of economic growth through reform. We need to raise total factor productivity”. 8

Supply-side structural reform will focus on unleashing and developing productive forces, advancing structural adjustment through reforms, reducing ineffective and low-end supply of goods and services, expanding effective and mid-to-high-end supply, enhancing the adaptability and flexibility of the supply structure to demand changes, and improving total factor productivity.9 Its main tasks are “cutting overcapacity, destocking, deleveraging, reducing corporate costs and shoring up weak spots”: (1) cutting overcapacity: eliminating backward excessive capacity, especially steel and coal production capacity; (2) destocking: reducing real estate inventory, especially in the third- and fourth-tier cities; (3) deleveraging: reducing the debt level of governments, enterprises and individuals; (4) reducing costs: reducing social costs, especially corporate costs; (5) shoring up weak spots: shoring up weak spots in public services, infrastructure and institutions.

It is necessary to understand the supply-side structural reform from the following aspects.10 First, there is a fundamental difference between supply-side structural reforms and Western supply-side economics. Supply-side economics emphasises tax cuts, overemphasises the role of tax rates, and has a relatively absolute ideological approach. It focuses only on supply but neglects demand, and focuses only on market functions while neglecting the role of the government. Supply-side structural reform involves not only the issues of taxes and tax rates, but also aims to address a series of problems in the supply side of China’s economy through a series of policy measures, particularly the policy measures to promote scientific and technological innovation, to develop the real economy and guarantee and improve people’s living standards. The reform not only emphasises supply but also pays close attention to demand and highlights both the development of productive forces and the improvement of relations of production. The reform enables the market to play a decisive role in resource allocation, gives better play to the governmental role, and needs to both focus on the present and look ahead to the future. From the perspective of political economics, the fundamentality of supply-side structural reform is to make China’s supply capacity better meet the ever-increasing and ever-escalating individualised material, cultural, and ecological needs of the broad masses of people so as to achieve the goal of socialist production.

Second, supply-side structural reform is an inherent requirement for rebalancing of supply and demand. At present and in a coming period, China will face “four declines and one increase” in its economic development, namely decline in economic growth rate, decline in the prices of industrial products, decline in profitability of enterprises, decline in fiscal revenue, and increase in probability of economic risks. The main contradiction of these problems is not cyclical but structural, and the supply structure mismatch problem is serious. Meanwhile, the principle aspect of the contradiction is on the supply side rather than on the demand side. The main problem in China is not that there is insufficient demand or no demand, but that the demand has changed while the supply of products has not changed, and the quality and services fail to keep up with the pace of change. The shortage of effective supply capacity has caused a serious outflow of spending power.

As it is difficult to solve the structural contradictions such as overcapacity by relying solely on stimulating domestic demand, we should give priority to improving the supply-side structure and focus on effectively addressing overcapacity from the production side, promoting the optimisation and reorganisation of industries, reducing the costs of enterprises, developing the emerging industries of strategic importance and modern service industries, increasing the
supply of public goods and services, and improving the adaptability and flexibility of the supply structure to changes in demand so as to realise a leap from a low-level balance between supply and demand to a high-level balance between supply and demand.

Third, the supply-side structural reform provides the endogenous power for sustained and healthy economic development. Since the beginning of the 13th Five-Year Plan period (2016–2020), China has continued to deepen the supply-side reform and achieved initial results in economic restructuring and upgrading. The continuous decline of China’s economic growth in the previous six years ended in 2017, and China’s GDP exceeded the threshold of 80 trillion yuan for the first time; the economic profits continued to increase, the total profits of the enterprises under the Central Government exceeded 1.4 trillion yuan for the first time, the increment and growth rate of economic profits hit the best level in five years, the unemployment rate fell to its lowest point in five years, and the ex-factory prices of industrial producers turned from negative to positive for the first time in five years; the conversion of the impetus for economic growth was accelerated, the contribution rate of consumer spending to economic growth reached 58.8%, an increase of nearly 4% compared with 5 years ago, and the added value of the service industry accounted for 60% of the GDP, an increase of 5% compared with 5 years ago; the export structure has been continuously optimised, and the main forces for export have changed from labour-intensive industries to technology-intensive industries, high-speed rail, marine equipments, nuclear power equipments and satellites have become new competitive industries for export; and the industrial structure is moving towards the mid-to-high end in a quicker pace. According to the Global Innovation Index of the World Intellectual Property Organisation, the China Innovation Index has risen from 34th in 2012 to 22nd in 2017.  

China’s economic restructuring and the Belt and Road complement each other

On the one hand, China’s economic restructuring will provide a sustainable driving force for the Belt and Road Initiative. Conceptually, the Belt and Road Initiative pursues the principle that all countries, big or small, rich or poor, can participate on an equal footing. However, in terms of responsibility, as the largest developing country and the second largest economy in the world, especially as the initiator of the Belt and Road Initiative, China will inevitably have to shoulder more historical responsibilities in the initial stage to ensure that the Belt and Road Initiative will enter a virtuous cycle in the context of a weak global economic recovery. This imposes stricter requirements on the “locomotive” role of China’s economic growth. As efforts to supply-side structural reform are beginning to deliver results, the endogenous power of China’s economic restructuring will be further enhanced, thus providing a sustainable driving force for the Belt and Road Initiative.  

On the other hand, the Belt and Road Initiative will provide a favourable external environment for China’s economic restructuring. First, it helps transform and upgrade the manufacturing industry. The Belt and Road Initiative will promote construction of infrastructure and transnational and inter-regional connectivity. This will not only increase the effective demand for building materials such as iron, steel, and cement in the countries along the Belt and Road and alleviate the problem of overcapacity in traditional Chinese industries, but also sharply increase the demand for various types of complete sets of equipments through cooperation in major projects for high-speed railways, ports, electricity, oil and gas, and communications, thus expanding overseas markets for the development of China’s high-end manufacturing industries.

More importantly, the Belt and Road Initiative promotes trade facilitation on the basis of connectivity, which will effectively promote the trade between China and other countries, thus
providing a broader space for the transition and upgrading of China’s manufacturing industry under the unfavourable conditions of weak global trade growth.\textsuperscript{13} In 2017, China’s trade volume with the countries involved in the Belt and Road Initiative reached 7.4 trillion yuan, a year-on-year increase of 17.8\%, which was 3.6\% higher than China’s foreign trade growth rate.\textsuperscript{14}

Second, it helps promote innovation and development of the service industry. China is the second largest trader in services in the world. In 2016, China’s total trade in services was US$657.5 billion, second only to the United States. However, China has set the goal of economic restructuring and upgrading that “By 2020, the amount of imported and exported services shall exceed US$100 million; the proportion of trade in services to foreign trade shall be further enhanced; and the global proportion of our trade in services shall be increased year by year”.\textsuperscript{15} Meanwhile, we should also actively exploit the emerging markets, especially the service industry market with broad prospects in the countries along the Belt and Road.

More importantly, China is strengthening financial cooperation with the countries along the routes under the Belt and Road framework and promoting unimpeded currency circulation and financial integration. A network of financial institutions and services is spreading out to support the Belt and Road Initiative through innovative financing mechanisms. China supports cultural exchanges and cooperation in various fields and at different levels to promote understanding between people. This will provide financial convenience and humanistic advantages for China’s service industry to “go global” and effectively improve the service industry’s innovation capability and international competitiveness.

Third, it is conducive to the optimisation and remodelling of the international labour division system. The global financial crisis in 2008 broke the grand global economic cycle in which the developed economies in Europe and the United States spent by borrowing, East Asian areas provided high savings, cheap labour and products, and Russia, the Middle East, Latin America and other countries provided energy and resources, and it prompted the rapid adjustment of the pattern of global division of labour and cross-border reallocation of capital. All the major economies in the world have sought to improve their position in the division of labour through structural adjustments and strive for a more favourable position in division of labour.

China is willing to use the Belt and Road Initiative as a cooperation platform to promote economic policy coordination among various countries, improve the level of connectivity, foster bilateral and multilateral cooperation with a broader scope and at a higher and deeper level, and build a new cooperation framework that is open, inclusive, balanced, and mutually beneficial. This helps China and other countries along the routes to raise their positions in the international division of labour in the process of optimising and reshaping the international division of labour system and the global value chain, and prevents the developed countries’ long-term “low-end lock-in” of developing countries by relying on their technology and capital advantages so as to effectively ensure a good international environment for China’s economic restructuring.

Notes

3 Ibid.
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5 Hold High the Great Banner of Socialism with Chinese Characteristics and Strive for New Victories in Building a Moderately Prosperous Society in all Respects, Hu Jintao’s report to the 17th National Congress of the Communist Party of China on October 15, 2007.


7 Ibid.

8 Secure a Decisive Victory in Building a Moderately Prosperous Society in All Respects and Strive for the Great Success of Socialism with Chinese Characteristics for a New Era, Xi Jinping’s report to the 19th National Congress of the Communist Party of China on October 18, 2017.


10 Ibid.


