

China's changing economy

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By all accounts, the economy of China has undergone profound changes over the last several decades. The changes began in the late 1970s, shortly after the death of Mao Zedong, and they have been accelerating in recent years. Since 1978, when Mao's successor, Deng Xiaoping, introduced the first market-oriented reforms, China has developed one of the most dynamic and fastest-growing economies in the world. With its opening to foreign trade and investment, its burgeoning stock markets, and its rapidly growing private sector, China is well on its way to becoming an advanced industrial nation, as well as a major player on the global economic scene. At the same time, as observers have noted, the changes have not come without costs, such as rising income inequality between the urban and rural areas, growing social unrest, and worsening environmental problems.¹

Signs of the changes in China's economy abound. They can be seen not only in the country's macroeconomic statistics, but also in the visual evidence available to a visitor. When making the journey from the United States to China, for example, a traveler may notice that the airports in Beijing and Shanghai differ little from those in New York, Washington, and Tokyo: each is a modern, high-tech facility that essentially doubles as a shopping mall, with many of the same kinds of international fast-food chains, boutiques, and other retail establishments. Such a traveler might be surprised at the hotel accommodations

available in most Chinese cities, with air-conditioning, cable television (including programming in English), Internet access, and personal amenities such as toothpaste, shampoo, and shower gel.

Similarly, a person visiting a major city in China sees many of the same indications of commerce and economic activity that he or she might discern in Western cities: highrise buildings form the skylines; commercial banks, real estate offices, and other financial institutions fill the central business districts; large department stores, boutiques, grocery stores, and restaurants provide shopping and refreshment in the downtown areas; taxis, trucks, private automobiles, motor scooters, bicycles, and pedestrians crowd the busy streets; and the ubiquitous street vendors—both licensed and unlicensed—hawk their goods on every corner. Indeed, almost any consumer product available in the United States today also can be found in China. But, in addition to the visible signs of prosperity and heightened economic activity, one sees also unemployment, inequality, poverty, and pollution.

Some statistical comparisons between the United States and China help put the size and potential of the Chinese economy into perspective.² Although the land areas of the two countries are roughly the same, China's population of 1.3 billion exceeds the U.S. population by about a billion people. Similarly, China's labor force—those working or looking for work—which reached nearly 800 million in 2005, is more than 5 times the size of the U.S. labor force. China's level of employment reached 744 million in 2003, and the official (urban) unemployment rate was 4.3 percent. In the same year, the U.S. economy employed 138 million people and the unemployment rate in metropolitan areas was 6.0 percent.³

China's real gross domestic product (GDP) grew a phenomenal 9.3 percent in 2005, while the U.S. economy's growth rate for that period was 3.5 percent. Measured in terms of purchasing power parity, China's GDP totaled \$8.2 trillion, or

about \$6,300 per capita. Even at the official exchange rate, China's GDP (\$1.8 trillion) ranked seventh in the world, just ahead of Italy's (\$1.7 trillion) and just behind France's (\$2.1 trillion). By comparison, U.S. GDP, second only to that of the European Union, rose to \$12.8 trillion in 2005 (\$12.5 trillion in purchasing power parity), or close to \$42,000 per capita.

China's economic reforms began in 1978, when many of its communes and collectives were dismantled and replaced with a "responsibility system," in which individual farmers were given greater choice over what they produce. Legislation passed the next year permitted foreign companies and other economic organizations or individuals to join with their Chinese counterparts to establish businesses in China. The reforms continued into the 1980s and 1990s and accelerated after 1994, when passage of the Company Law laid the groundwork for Western-style corporate structures.

Another important milestone came in 1997, when the 15th Party Congress voted to allow many struggling State-owned enterprises (SOE's) to go bankrupt. Two years later, a constitutional amendment granted the private sector equal status with SOE's. Next, in perhaps the most striking display of its commitment to being part of the world economy, China gained entry into the World Trade Organization in 2001. Then, in 2004, the Chinese government guaranteed private property rights in its Constitution, further paving the way toward a full-scale market economy.

Employment trends in China over the last several decades provide further evidence of the manifold changes that have occurred since the economic reforms began.⁴ According to China's National Bureau of Statistics (NBS), the nation's economy employed 402 million people in 1978, more than two-thirds of whom worked in *primary industries*—farming, forestry, animal husbandry, and fishing. By 2003, the level of employment had risen to 744 million, an increase of 85 percent, or about 3.5 percent per year. During that 25-year period, the share of em-

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ployment held by primary industries dropped from 71 percent to 49 percent, while the share held by *secondary industries* (mining, manufacturing, and construction) increased from 17 percent to 22 percent and the share held by *tertiary industries* (finance, insurance, real estate, wholesale and retail trade, and services) increased from 12 percent to 29 percent. A 2002 *Monthly Labor Review* article by Ming Lu and others concludes that one of the main reasons for the strong growth in the tertiary industries is increased privatization, which they argue is easier in such tertiary industries as trade and services, due to fewer restrictions and lower startup costs.⁵

In terms of employment, China's manufacturing industry is the largest in the world. In a 2005 article in the *Monthly Labor Review*, Judith Banister examines manufacturing employment during the 1978–2002 period.⁶ Banister argues that China's official estimate of 83 million manufacturing workers in 2002 probably is understated, with the actual figure closer to 109 million. For perspective, in the same year, the Group of Seven (G7) major industrialized nations—Canada, France,

Germany, Italy, Japan, the United Kingdom, and the United States—employed a combined total of 53 million manufacturing workers. Thus, even by the official estimate, China's manufacturing employment exceeds that of the entire G7 by 30 million workers. Despite the large numbers, however, the industry has experienced considerable restructuring in recent years, as the effects of productivity gains and privatization have begun to take hold, leaving many workers unemployed.

To take up the slack from failing State-owned enterprises and other businesses shedding workers, the Chinese government has been encouraging entrepreneurship and self-employment by relaxing some of the registry requirements for starting a business and by providing training. China's NBS estimates that the share of total employment in SOE's in 1978 was around 19 percent (75 million workers); by 2003, that figure had fallen to about 9 percent (69 million workers). By contrast, the number of self-employed workers and the number employed in private enterprises, both of which barely registered in 1978, had grown to 46 million and 43 million, respectively, by 2003.⁷

Two other areas that demonstrate China's changing economy are international trade and foreign direct investment (FDI).⁸ China exported \$752.2 billion worth of goods in 2005, while importing \$631.8 billion. More than a fifth (21.1 percent) of those exports went to the United States, 17 percent went to Hong Kong, and 12.4 percent went to Japan. FDI in China reached \$153 billion in new agreements in 2004. Hong Kong was the principal investor (\$19 billion), followed by the British Virgin Islands (\$6.73 billion), South Korea (\$6.25 billion), Japan (\$5.45 billion), and the United States (\$3.94 billion).

Closely related to both international trade and FDI are the so-called special economic zones (SEZ's)—areas with lower taxes, fewer legal restrictions, and other incentives designed to encourage foreign investment and increase international trade. The SEZ's generally import components, raw materials, machinery, and other inputs to produce finished goods, primarily for export. Although these areas represent only a fraction of China's overall economy, they are an important part of the country's effort to become integrated into the global economy. □

Notes

¹ For more on the costs of China's economic reforms, see Wayne M. Morrison, "China's Economic Conditions," CRS Issue Brief for Congress (Congressional Research Service, March 17, 2006), pp. 10–12.

² The data cited in this and the subsequent paragraph are from the CIA's *World Factbook: 2005* (Central Intelligence Agency, 2005); on the Internet at <http://www.cia.gov/cia/publications/factbook/index.html>.

³ The overall unemployment rate in the

United States in 2003 also was 6.0 percent.

⁴ The data cited in this paragraph are from *China Statistical Yearbook: 2004* (National Bureau of Statistics of China, 2004); on the Internet at <http://www.stats.gov.cn/english/statisticaldata/yearlydata/yb2004-e/indexeh.htm>.

⁵ Ming Lu, Jianyong Fan, Shejian Liu, and Yan Yan, "Employment restructuring during China's economic transition," *Monthly Labor Review*, August 2002, pp. 25–31.

⁶ Judith Banister, "Manufacturing employment in China," *Monthly Labor Review*, July 2005, pp. 11–29.

⁷ *China Statistical Yearbook: 2004*.

⁸ Data on imports and exports are from *World Factbook: 2005*; data on foreign direct investment are from "Foreign Investment in China" (Washington, U.S.-China Business Council, 2005); on the Internet at <http://www.uschina.org/statistics/2005foreigninvestment.html>.