

ECONOMICS

China is no Japan

by Alessandro Magnoli Bocchi

thegulf@tradedearabia.net



REMEMBER Japan in the 1980s? It seemed unstoppable: wealthy and dynamic, able to produce better and cheaper products than the rest of the world, it became an export powerhouse and accumulated huge dollar surpluses. For more than a decade, the growth in Japan's real gross domestic product persistently exceeded that of the US. The Tokyo stock market set record after record. The hard-working Japanese were winning a large number of "western" jobs, and Japan's large corporations relentlessly acquired companies in the US and Europe. Japan, having surpassed Germany in the mid-1970s, was the world's second-largest economy and seemed on track to effortlessly overtake that of the US. In short, Japan was a rising superpower, widely perceived as becoming the leader of the global economy.

Then, in the 90s, this vertiginous rise suddenly stopped. A prolonged economic stagnation sapped Japan's optimistic expectations. Why? Because the stock market and real estate bubbles burst – one after the other – in 1990 and 1991. The result was an 80 per cent collapse in asset prices, a troubled financial system, and a credit crunch. Despite a massive fiscal expansion – the government spent more than \$2 trillion on public works – and the socialisation of losses, the 1990s was a lost decade. Still an economic power, Japan has lost regional economic leadership to China.

Today, it is Japan's neighbour

who occupies the role of megapower in the making. It looks as invincible as the Japanese did in the 80s. It has already surpassed Japan as the holder of the largest foreign exchange reserves in the world, and nine-out-of-every-10 tonnes of steel produced globally end up in its construction sites. As Asia's economic hub, China is driving the region's economic integration. With its low wages and abundant foreign direct investment, it has the potential to become the world's largest consumer market. According to forecasts, in 2010 the Chinese economy will overtake Japan as the world's second-largest economy. By 2025, it will have left the US behind. By 2050, it may even surpass the combined production of the western hemisphere.

Could China experience the same fate as Japan and undergo a prolonged recession or depression between now and 2020? 'No', is the short answer. Present-day China is as dynamic as Japan was in the '80s, but it is far less wealthy. Its economy is at an earlier stage of development, and that is a blessing: starting from a much lower base, it can absorb inefficiencies – and still achieve strong and sustainable growth over the medium term.

Doubtless, the two economic systems are quite alike. Japan and China rely on export-led growth and their economies also feature highly subsidised and protected sectors, where firms – shielded from shareholders and market pressures – become less and less account-

able, transparent, and innovative. Both economies enjoy high saving and low consumption rates, which supply abundant capital in the form of bank loans.

Still, China is different. Its ongoing economic dynamism seems sustainable in the longer term. Firstly, China has strong fundamentals: excellent demographics, a rising middle class, massive urbanisation, and high savings. If coupled with the benefits of free trade, market reforms, and economic integration, these fundamentals will bring about higher salaries and an increased standard of living.

China is also trying to avoid export-dependence and is engaged in the expansion of domestic private consumption. During the 1990s, Japan was unable to reconfigure its economy away from the export-led model, but Chinese policymakers are already promoting local demand, and actively considering structural reforms, including the modernisation of tax and financial systems and establishment of social protection schemes.

Japan's unprecedented rise was based largely on inflated property prices. In China – while there are signs of excessive bank loans and unproductive investments – there are no bubbles on the scale of Tokyo in the 1980s.

While vested interests representing inefficient sectors of its economy hampered reforms in Japan, in China – a country undergoing huge social changes, including rising inequality and massive migration to the cities – the Communist Party knows its legitimacy rests on delivering consistent annual increases in prosperity.

The possibility of a decade-long stagnation seems unlikely in China in the near-term. The country is more likely to strengthen its position in the world economy. ■

Alessandro Magnoli Bocchi is chief economist at the Kuwait China Investment Company (KCIC).

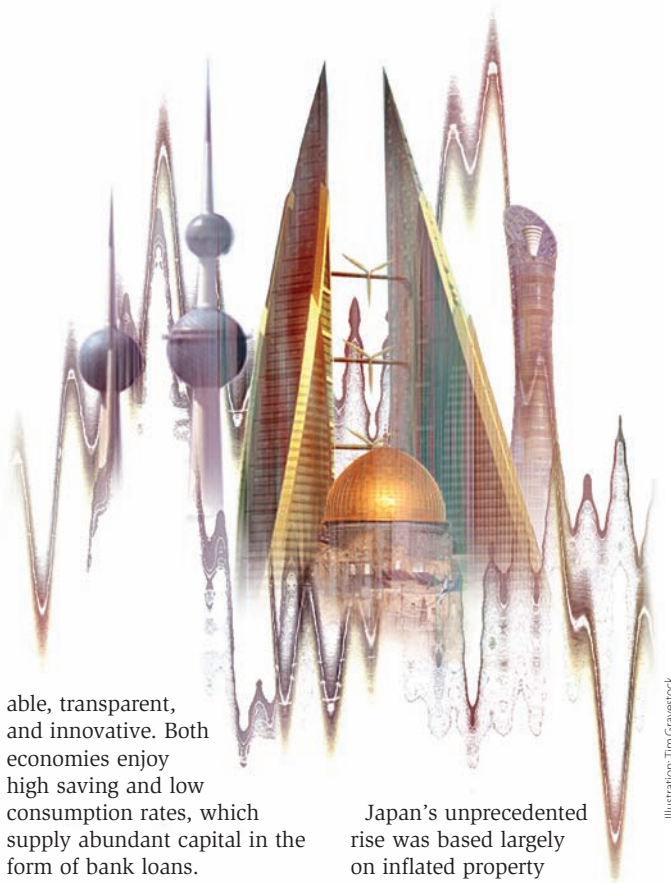


Illustration: Tim Gravestock

Any news? Any views? Email managing editor Stan Szczowka – stang@tradedearabia.net – YOUR OPINION COUNTS