Navigating China's Economic Development in the New Era

From High-Speed to
High-Quality Growth

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Abstract: China's economy has entered a "new normal," transforming from high-speed growth to high-quality development. In the new era, China does not only need to shift its path of development in a timely fashion, but it should also take bigger steps to modernize its economic system. Facing various new demands and challenges, China must make every effort to foster an economic system that features innovation-driven industries, urban-rural and regional coordination, a market economy with socialist characteristics, as well as lasting momentum for opening-up on all fronts. It is expected that despite the economic difficulties at the moment, China will accelerate its economic transformation to achieve high-quality development and make new contributions to the world economy.

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China has entered a new era of development with its economy shifting to a “new normal,” marked by a moderate growth rate and rebalancing of the economy toward consumer spending and technological innovation.¹ The structural changes and new features of China’s economy under the new normal are not only a result of the sluggish recovery of the world economy since the 2008 global financial crisis, but also a response to the ever more prominent challenges for the unbalanced, uncoordinated and unsustainable development over the past decade. In view of the fact that China’s long-, mid- and short-term economic cycles overlap at this critical moment,² it is necessary to fully examine the strengths and weaknesses of China’s economy after more than two decades of rapid growth, so as to map out a viable way for the deepening reform and further development of China’s economy.

In fact, during the past five years, the Chinese government has already formulated macroeconomic policies based on a thorough assessment of the new normal. Most significantly, the 19th National Congress of the Communist Party of China (CPC) held in late 2017 laid out a clear blueprint for further modernizing China’s economic system in the following 10 to 20 years. In order to facilitate the transition from high-speed growth to high-quality development, a number of major policies are being made to promote China’s reform and opening-up more expansively, while maintaining economic stability against the current turbulence in global trade as well as disputes with regard to the existing economic institutions like the World Trade Organization (WTO).

Based on Chinese President Xi Jinping’s work report to the 19th CPC National Congress, this article aims to project the future trajectory of China’s economic development and reform of its economic system under

¹“Full text of Chinese President Xi’s address at APEC CEO Summit,” Xinhuanet, November 11, 2014, http://www.xinhuanet.com/english/2017-11/11/c_136743492.htm.

²Liu Yong, “Zhongguo zheng chuyu sanchong jingjizhouqi chongdie guankou [China is at a Critical Moment with Three Overlapping Economic Cycles],” Phoenix News, April 9, 2014, http://news.ifeng.com/gundong/detail_2014_04/09/35584505_0.shtml.

the new normal. The first two sections analyze China's economic achievements over the past few years under the new normal and the implications of China's economic transformation; the third discusses major goals of China's economic development and reform in the new era; and the fourth elaborates on the viable approaches for China to achieve those goals. It concludes that China's economy has taken a new path towards high-quality development, which requires substantial upgrade of the whole economic system in a timely yet stable way.

China's Economic Achievements Under the New Normal

Over the past few years, China's economic development has largely been following a path different from the previous decades, with its economy entering a stage widely known as the "new normal." The new normal has been characterized by a slowdown in economic growth, accelerating re-adjustment of the economic structure, and change of the main economic driver from investment to consumer spending and innovation. Since the 18th CPC National Congress held in November 2012, the five core concepts — "innovation, coordination, green development, opening-up and sharing"³ — have been advocated and implemented in China's economic development, as the government speeds up the structural reform "on the supply side." Most remarkably, the CPC leadership has many a time reiterated that it is the market that should play a decisive role in resource allocation, while the government can better serve its duty in a market-oriented economic system.

Under the new normal, the coordination among economic growth, quality, and efficiency has been highly addressed, with the aim to promote the total-factor productivity as well as to improve the quality and efficiency of economic growth. Step-by-step, China has been pressing on with a series

³The Fifth Plenary Session of the 18th CPC Central Committee stressed that it is necessary to firmly establish and effectively implement the development philosophy of innovation, coordination, green development, opening-up and sharing, to achieve the development goals during the "13th Five-Year Plan" period. See "Xinhua Insight: China to Start Reform Focused on Quality of Life," Xinhuanet, December 11, 2015, http://www.xinhuanet.com/english/2015-12/11/c_134907652.htm.

of new strategies and measures including the “Belt and Road Initiative (BRI),” the coordinated development of the “Beijing-Tianjin-Hebei (Jing-Jin-Ji) Region,” the construction of the “Yangtze River Economic Belt,” and the development of the “Guangdong-Hong Kong-Macao Greater Bay Area,” among others. These new strategies and measures have promoted China’s economy by fostering new growth drivers and expanding development space. As a result, China’s economic development has increasingly embarked on an approach toward higher quality, better efficiency, more fairness, and greater sustainability.

Although significantly lower than the double-digit growth in almost each year during the first decade of the 21st century, China managed to achieve an average annual growth rate of more than 7 percent from 2012 to 2017; its Gross Domestic Product (GDP) increased from 54 trillion Renminbi (RMB) to 80 trillion, contributing over 30 percent to the world’s total economic growth during the same period.⁴ In the meantime, China’s foreign trade volume reached 27.8 trillion RMB, or about 4.2 trillion USD, in 2017, nearly 8.5 percent higher than the number in 2012, accounting for almost a quarter of the world’s total.⁵ As such, China has been widely recognized as a major engine of world economy.

China’s strong economic performance has generated a great amount of wealth. The country’s foreign exchange reserves have exceeded 3 trillion US dollars, and the disposable income of urban and rural residents

China will maintain robust economic growth while seeking high-quality development.

⁴Xi Jinping, “Build a Moderate Prosperous Society in all Respects, and Strive for New Victories of Socialism with Chinese Characteristics,” in Xi Jinping, *The Compilation of Documents of the 19th National Congress of the Communist Party of China* (Beijing: People’s Publishing House, 2017).

⁵Ministry of Commerce of the People’s Republic of China, “*Zhongguo duiwai maoyi xingshi baogao (2018 nian chunji)* [Report on China’s Foreign Trade Situation, Spring 2018],” <http://zhs.mofcom.gov.cn/article/cbw/201805/20180502740111.shtml>; and Ministry of Commerce of the People’s Republic of China, “*2012 nian zhongguo duiwai maoyi fazhan qingkuang* [Development of China’s Foreign Trade in 2012],” April 28, 2013, <http://zhs.mofcom.gov.cn/article/Nocategory/201304/20130400107790.shtml>.

increased at 7.4 percent annually from 2013 to 2016, a little higher than its GDP growth, meaning that the general households have benefited from China's economic growth. For many years, the consumer price index (CPI) has remained rather stable, ranging from 1.4 percent to 2.6 percent, without large fluctuation, which helps both industries and residents maintain their confidence in the long-term projection of China's economic development.

In addition, the past six years have witnessed an accelerated process of urbanization in China, thanks to which about 80 million rural residents have become urban residents. In terms of poverty reduction, 13 million Chinese people were lifted beyond the national poverty line every year during the past six years.⁶ Clearly, China's economic growth and social development under the new normal has facilitated its shift from high-speed growth to high-quality development.

Implications of China's Economic Transformation

While China's development has entered into a new era, its economy is facing new challenges and tasks. Above all, China's past economic achievements have laid a solid foundation for its further reform and opening-up. Compared with two decades ago, China's social productivity has greatly improved. Notably, the country has become the world's second largest economy since 2010, ranking top three in terms of total trade volume as well as inbound and outbound investment. As the "world factory," China has maintained a powerful manufacturing sector with the greatest added value for seven consecutive years. It is also worth mentioning that China has been leading the world in production capacity of over 220 major industrial and agricultural products. It is widely acknowledged that China's improved productivity and enormous market potential will not only facilitate the country's development in the new era, but also generate lasting momentum for the world economy as well. Since its productivity has been greatly enhanced, China is now faced with new

⁶Bureau of Theoretical Studies of the CPC Publicity Department, *Face to Face with the New Age* (Beijing: Study Press/People's Publishing House, 2018).

demands for its economic transition — from an emphasis on size to that on quality.

Next, although the living standards of the Chinese people have significantly risen over the last four decades, with the per capita income continuing to rise and the Engel Coefficient⁷ having dropped from nearly 0.5 in the late 1990s to below 0.3 in 2017,⁸ the issue of unbalanced and inadequate development has been increasingly salient. In fact, President Xi identified the issue in his work report to the 19th CPC National Congress as the “principal contradiction,” or greatest challenge, to Chinese society in the new era.⁹ The issue of unbalanced and inadequate development should not be observed only in terms of spatial or regional distribution of economic productivity, but it is also closely related to the industrial structure, urban and rural disparities, income gaps, and the mismatch between supply and demand. In general, China is still lagging behind developed economies in social, cultural, and ecological development. Thus, it is of great importance for China to transform its model of economic development and build a modernized economic system by adapting to new demands and requirements of the principal contradiction for its social development. To achieve the goal of building a moderately prosperous society by 2021, the Chinese government has been revamping the national social security network, which is now covering more urban and rural residents in a broader range of areas. At the same time, more work is required to better serve the public’s needs

Inadequate and unbalanced development has become the biggest challenge for China.

⁷The Engel Coefficient, or Engel’s Law, is a statistical term that states that when income rises, the percentage of income spent on food decreases. It is commonly used to reflect the living standard of a country. The higher the Engel Coefficient, the poorer the society, and vice versa.

⁸Zhu Yu, “Zhongguo engeerxishu shoupo 30%, Xiaoshuzi zheshe dabianqian [Chinese Engel’s Coefficient Dropped Below 30% for the First Time, Indicating Major Changes],” *National Business Daily*, April, 17, 2018, <http://www.nbd.com.cn/articles/2018-04-17/1208816.html>.

⁹Xi Jinping, Work Report to the 19th National Congress of the Communist Party of China, October 18, 2017, http://www.chinadaily.com.cn/china/19thcpcnationalcongress/2017-11/04/content_34115212.htm.

for higher levels of democracy, fairness, justice, security, and environmental protection.

Finally, China's global status has been profoundly enhanced since its reform and opening-up began in the late 1970s. The increase of its comprehensive national power as well as its growing role as the world's major economy requires China to speed up its economic modernization, especially the transformation of its economic system, in the new era. As the world's largest developing country, China will continue taking the lead in the developing world, showing respect for other developing nations including the least developed countries (LDCs), so as to shape a friendly international environment beneficial for itself and the common development of the world.

China's Development Goals in the New Era

Given the new social demands and the objective of building a strong nation, China needs to adjust its development path in the following ways. The first is to achieve the transition from growth orientation to all-round development. Theories of development economics show that economic growth is different from development in that the latter usually carries more comprehensive and sustainable meanings and requirements. For example, a country with a high GDP growth rate but poor performance in environmental protection can hardly maintain its growth, because the potential costs of pollution will accumulate and slow down the economic growth in the long run. Therefore, China needs to pay more attention to the quality of its economic growth, speed up the upgrade of its economic structure and achieve coordinated development of its political, cultural, social and ecological environments. This requires China to fully implement the five development concepts of "innovation, coordination, green development, opening-up and sharing."

Secondly, China needs to realize the transformation from growth in quantity to growth in quality and efficiency. Theories of economic growth indicate that long-term growth mainly depends on the total-factor productivity. In other words, it is necessary to improve the efficiency of resource allocation and the rate of technological progress. In the past, China's comparative advantage of low-cost labor and land usage did stimulate the country's economic growth, but it has largely locked China up in a

relatively low position along the global value chain. Facing ever more intense competition on the global market, China must transform its economy from factor-driven growth to efficiency- and innovation-driven development, the key to which is to vigorously implement its innovation-driven strategies and enhance the all-round quality and efficiency of development.¹⁰

The third way is to accelerate its shift from being merely a big economy to becoming a competitive economy. Theories of international economics and global value chain suggest that a country's position in the global value chain is key to its overall competitiveness. Today, that position is less determined by the international division of labor, comparative advantages, or resource endowments, than by its innovation capacity, since traditional indicators like huge market size, large trading volume and so on no longer represent the competitiveness of a country in the international market. Although China is a big economy and a major trading country, there is still a long way to go before it becomes a strong nation in trade, finance, investment and, most importantly, economic quality.

The fourth way is to catalyze the change of China's role from being a rule taker to becoming a rule maker in the international system. Like in the case of Great Britain in the 19th century and the United States after World War II, the key for a big-sized economy to grow into a strong and competitive economy lies in whether it can fully participate in the global governance system and join in the formulation of global rules on trade, investment and other related issues. During the past decades, China has remained largely a recipient of existing international rules and regulations mainly designed by advanced economies. However, some rules and regulations have turned out to be obviously unfair or outdated, thereby requiring modification. In the new era, China should play a more active role in the rule making process at the global level and, when necessary, speak up for other developing countries. At present, China is actively participating in various international organizations, hosting international

Profound economic transformation is needed for China to enhance its global competitiveness.

¹⁰Quoted from the CPC Central Economic Work Conference which took place on December 18–20, 2017.

conferences on cooperation, and providing all kinds of aid and support for the LDCs. Under the framework of the United Nations, Chinese medical teams and peacekeeping forces are also fulfilling their responsibilities and have earned a good reputation for China. With regard to the current disturbance in international politics and global trade, it is of particular importance for China to work closely with countries of the willing to uphold the stability and integrity of major global governance institutions like the WTO.

New Approaches of China's Development

China's economic transition calls for deepening reforms that facilitate growth of higher quality and efficiency. Building up a modernized economic system is crucial to consolidating China's economic power in this respect.¹¹ In the future, China is expected to adopt the following approaches to address the most daunting challenge of unbalanced and inadequate development and to realize its economic transformation.

First of all, China will continue to implement in-depth change via supply-side structural reforms and develop a modernized economic system based on the principles of high quality and high efficiency. Priority will be given to the improvement of quality in the supply system, focusing on the real economy, for only economic growth from better quality and higher efficiency by thorough reforms will enhance total-factor productivity in reality.

To begin with, China will aim to become a strong manufacturer with the development of advanced manufacturing and implementation of the "Made in China 2025" Initiative.¹² In other words, China will become a "world factory" not only in quantity, but in quality as well. That requires China to place more emphasis on both technological progress and technical talents. Thus, China needs to promote further integration of the internet, big

¹¹Xi Jinping, "Build a Moderate Prosperous Society in all Respects, and Strive for New Victories of Socialism with Chinese Characteristics."

¹²The "Made in China 2025" Initiative is a ten-year guideline issued by the Chinese government for enhancing the manufacturing sector of the country. First proposed in March 2015, the Initiative became an official guideline in May 2015, highlighting nine strategic tasks and national support in eight aspects. See more information on <http://www.gov.cn/zhuanti/2016/MadeinChina2025-plan/>.

data, and artificial intelligence (AI) with the real economy, in order to foster a green and low carbon economy, modern supply chains, and human capital services. In the meantime, China's business climate needs to be optimized, and a sense of innovation and entrepreneurship further encouraged, with proper policy incentives and legal protection, which would help create new momentum for the market and generate more opportunities for employment.

Next, China will endeavor to upgrade its traditional industries along the global value chain with stronger policy support, which also requires the improvement of the basic economic infrastructure. In this way, some low value-added industries and jobs can be transferred to Central and West China, allowing the land in East China to be freed up for higher value-added industries. This step is key not only to facilitate industrialization and urbanization in Central and West China, but also to rebalance regional development across the country.

Furthermore, China will continue its efforts to cut overcapacity, de-stock and de-leverage, so as to improve the efficiency of resource allocation, strengthen the core competitiveness of industries, and ensure the sustainability of economic growth. At present, efforts are mainly concentrated on such heavy industrial production as steel, coal, cement, electrolytic aluminum, plate glass, and shipment facilities. In the future, they may extend to certain fields of light industrial production that lack international competitiveness and risk pollution of the environment.

Secondly, China will carry on with innovation-driven development and go all out to build an innovation-oriented economic system. Improving labor productivity is the key to speeding up the development of a high-quality economy, and the implementation of China's efficiency-driven and innovation-driven strategy can inject new impetus into the modernized economic system. To be more specific, China will continue to encourage investment in research and development (R&D) to build a strong economy in science and technology, product quality, aerospace, cyberspace and transportation. It does not mean that China will adopt an import-substitution policy, by which developing economies gradually replace imports with domestic production. Rather, China's involvement in globalization and its industrial and technological development require the country to participate more actively in international cooperation on innovation. To do that, China must accelerate its own progress on technological innovation.

With cutting-edge technologies, China can form new comparative advantages in its industrial sectors, thus securing its desired quality-oriented economic growth in the long term.

Innovation will play a vital role in China's economic transformation.

Meanwhile, China will also develop a market-oriented system that encourages technological innovation, in which enterprises are the main players and synergy is created through joint efforts of enterprises, universities, and research institutes.¹³ China needs to expand the spillover effect of sci-

entific and technological innovation and encourage the application of such innovation. In cooperation with universities and research institutions, industrial sectors can make better application of the technological progress to meet market demands.

The Chinese government must also remain open to leading innovation while mustering scientific and technological innovation resources and elements in the global market, and trying different models of technological cooperation across borders. Further integration of the urban and the rural areas is also necessary for strengthening technological and capital accumulation in the agricultural sector, which will greatly increase added value for rural industries.

Thirdly, China will pursue a rural revitalization strategy and build a modern system of agricultural economy that serves the integration of urban and rural areas. As China's urbanization process depends largely on the development of the rural areas and agricultural modernization, more effort will be made to encourage urban internal factors to flow to the countryside, which would help realize two-way flow of production factors and achieve integrated urban-rural development eventually. In order to revitalize rural industries, rural talents, rural culture and ecology for the integrated development, the crucial step is to advance reforms of the rural land system, separating the ownership rights, contract rights, and management rights for contracted rural land. Like the epoch-making reform and opening-up four decades ago, this key step will not only inspire the working enthusiasm of rural

¹³Xi Jinping, *Xi Jinping on Socialist Economic Construction* (Beijing: Central Literature Publishing House, 2017).

residents, but also create opportunities for institutional improvement of the agricultural sectors.

Another step is to establish modern agricultural systems including the production system, business operation system, and agricultural service system. It is necessary to develop appropriately scaled agricultural operations of various forms, cultivate new types of agri-business, and improve specialized agricultural services, so as to enhance the efficiency and energy of the agricultural sector. Besides, the integrated development of primary, secondary, and tertiary industries needs to be further encouraged in rural areas so that the income of rural residents can increase on par with that of urban residents.

Similarly, the reform of the Chinese factor market (such as the labor market, the capital market, and the raw materials market) needs to be further advanced and entrenched, in order to promote the free flow of labor, capital, talents and other resources between urban and rural markets. That is indeed a critical step toward overcoming the principal challenge of unbalanced development between urban and rural regions in China.

Fourthly, China will continue to implement a coordinated regional development strategy. Many new strategies and initiatives of coordinated development among regional economies have been proposed over the past few years. Among them are the three major regional economic development strategies including the Beijing-Tianjin-Hebei Region, the Yangtze River Economic Belt, and the Guangdong-Hong Kong-Macao Greater Bay Area, apart from the global development-oriented Belt and Road Initiative. More aid will be given to the development of the historical bases of support for the CPC, most of which are located in the hinterland or border regions, with a large number of ethnic minorities. While encouraging East China to take the lead in pursuing optimal development through innovation, new measures will be adopted to accelerate the revitalization of traditional industrial bases in Northeast, Central and West China, so as to narrow the development gaps across China.

In addition, the Chinese government will lead efforts in creating city clusters to enable coordinated development of cities of different sizes, together with small towns, such as the city clusters in the Yangtze River Delta in East China and the Pearl River Delta in South China. In the meantime, China has adopted a forward-looking and comprehensive plan with high standards to build the Xiong'an New Area in North China, in order to

relieve Beijing of functions nonessential to its role as the capital.¹⁴ These measures will serve as new growth drivers in the coordinated development of regional economies, which would both help rebalance the internal development within each region and upgrade the cooperation framework among different regions.

Fifthly, China is expected to strengthen efforts to improve the socialist market economy and build a modern, market-oriented economic system. To do that, China must ensure that the market plays a decisive role in allocating resources and that substantial reform is conducted to provide equal conditions and effective incentives for all kinds of market entities, whether state-owned, private, or foreign-funded enterprises. China needs to improve existing law and regulations while strengthening the protection enforcement mechanism for different property rights. At present, it is of urgent importance to reform the mixed ownership system of state-owned enterprises, so as to promote the development of national capital and foster world-class enterprises with global competitiveness.

Moreover, China should speed up its market-based reform of economic factors and develop a unified, competitive, and modernized market system to improve market performance, including preventing price distortion and enhancing market efficiency, among other things. A strong macro-control framework must be built through sound monetary and macro-prudential policies to guard against various economic risks and strengthen the confidence of other countries in the sustainability of the Chinese economy. China's income distribution system should also be upgraded for more equity, justice, shared development and common prosperity, in order to fulfil the CPC commitment of "leaving no one behind" on the path of China's lasting development.

China's economic transition calls for a comprehensive upgrade of its economic system.

Finally, China will seek to break new ground in pursuing opening-up on all fronts. The building of socialism with Chinese characteristics in the new era requires China to establish an open economy with higher standards to meet the new trends of

¹⁴Xi Jinping, "Build a Moderate Prosperous Society in all Respects, and Strive for New Victories of Socialism with Chinese Characteristics."

development in international trade and investment, and to improve its own competitiveness while embracing challenges from the international market with more confidence and self-discipline. International cooperation on innovation should be particularly encouraged to improve the quality and efficiency of the economy. In this light, it is crucial for China to adhere to the principle of win-win cooperation for shared growth, in contrast to the self-interested stance and unilateral approach of some national governments like the Trump administration. Indeed, China is a beneficiary of globalization, and it thus sees globalization as a lasting and irreversible trend. In the future, China will keep striving for deeper integration with the world economy toward common and higher-quality development.

A most important indicator of China's resolution to build an open economy is to observe how it is going to further implement the Belt and Road Initiative. For instance, will it use the Initiative mainly to shake off its industrial overcapacity or to promote the common development of related countries? Does it aim to enhance its geostrategic influence on the expanse of the Initiative or to truly strengthen interconnectedness of the world? The Chinese government has made it clear that by realizing the "five types of connectivity," namely policy co-ordination, facilities connectivity, unimpeded trade, financial integration, and people-to-people bonds, China will keep on integrating with the world economy through such mechanisms as the Belt and Road Initiative.¹⁵ Yet the long-term effect of the Initiative remains to be seen.

With regard to the ever more intense trade disputes around the world, China will also strive to be a strong trading nation while rebalancing its trade relationships with major trading partners like the United States. Apart from promoting substantial changes in its trade development model as well as enhancing the added value and competitiveness of its products, China must persist in opening up its service sector and accelerate the transformation of its service industry, focusing on such fields as finance, education,

¹⁵*Vision and Action for Promoting the Joint Construction of the Silk Road Economic Belt and the 21st Century Maritime Silk Road* (Beijing: National Development and Reform Commission/Ministry of Foreign Affairs/Ministry of Commerce, June 2014).

health care, culture and tourism, among others, in order to promote their "opening, innovation and integrated development with the manufacturing sector."¹⁶

At the same time, China needs to accelerate the reform of government institutions and mechanisms so as to build a service-oriented government on the principles of "decentralization, supervision by law, and better service for the people." To follow up with the dynamic trends of international investment and trade, the Chinese government must make greater effort to foster a favorable business climate for both domestic and foreign investment. High-level investment and trade facilitation policies should be made to implement the pre-establishment national treatment and the negative-list management, so as to protect the legitimate rights and interests of foreign investors. Besides, it has been five years since the China (Shanghai) Pilot Free Trade Zone was established in September 2013, with much progress achieved and experiences gained. In the future, China should speed up the construction of such free trade zones and ports, at least in the relatively more developed regions in East and South China, to more closely integrate its economy with the world.

Conclusion

In view of the changing domestic demands and challenging situation of international trade and cooperation, high-quality development is a necessary direction for China's further reform and opening-up. As high-quality growth depends on a modern economic system, the key to the transformation from rapid growth to high-quality development lies in the building of such a modern economic system by promoting innovation, strengthening property rights protection and fair competition, as well as enhancing the free flow of economic factors and their efficient allocation.

¹⁶Ministry of Commerce of the People's Republic of China, "Zhongshan buzhang zai diwujie jingjiaohui quanqiu fuwumaoyi fenghui shang de zhici [Minister Zhong Shan Addresses Global Service Trade Summit on the Fifth China Beijing International Fair for Trade in Services]," May 31, 2018, <http://coi.mofcom.gov.cn/article/y/gnxw/201805/20180502750507.shtml>.

Entering into the new era, China's economic performance and its transition to high-quality development will generate profound impact on the structural and sustainable development of the world economy. Considering the turbulent international political and economic situation at present, the direction and approaches to China's high-quality development are worthy of closer observation and more in-depth analysis.