ChinaComment

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Current-account surplus to shrink

China's current-account surplus — the combination of its trade surplus and its net income from foreign investments — is the largest in the world. With a trade surplus of $190 billion and the income from its nearly $3 trillion portfolio of foreign assets, China's external surplus stands at $316 billion, or 6.1 percent of annual GDP.

Because the current-account surplus is denominated in foreign currencies, China must use these funds to invest abroad, primarily by purchasing government bonds issued by the United States and European countries. As a result, interest rates in those countries are lower than they would otherwise be.

However, that may all be about to change, as the policies that China will adopt as part of its new five-year plan will shrink its trade and current-account surpluses.

In any country, the current-account balance is the difference between national savings and national investment in plant and equipment, housing, and inventories. This key fact is not a matter of economic theory or a historic regularity. It is a fundamental national-income accounting identity that must hold for every country in every year. So any country that reduces its saving without cutting its investment will see its current-account surplus decline.

It is possible that, before the end of the decade, China's current-account surplus will move into deficit, as the country imports more than it exports and spends its foreign-investment income on imports rather than on foreign securities. If that happens, China will no longer be a net buyer of US and other foreign bonds, putting upward pressure on interest rates in those countries.

Although this scenario might seem implausible at present, it is actually quite likely to occur. After all, the policies that China will implement in the next few years target the country's enormous saving rate — the cause of its large current-account surplus.

China's national saving rate — including household saving and business saving — is now about 45 percent of its GDP, which is the highest rate in the world. But, looking ahead, the five-year plan will cause the saving rate to decline, as China seeks to increase consumer spending and therefore the standard of living of more Chinese citizens.

The plan calls for a shift to higher real wages so that household income will rise as a share of GDP. Moreover, state-owned enterprises will be required to pay out a larger portion of their earnings as dividends. And the government will increase its spending on consumption services, such as health care, education, and housing.

These policies are motivated by domestic considerations, as the Chinese government seeks to raise living standards more rapidly than the moderating growth rate of GDP. Their net effect will be to raise consumption as a share of GDP and reduce the national saving rate. And with that lower saving rate will come a smaller current-account surplus.

Since China's current-account surplus is now 6 percent of its GDP, if the saving rate declines from the current 45 percent to less than 39 percent — still higher than any other country — the surplus will become a deficit.

This outlook for the current-account balance does not depend on what happens to the renminbi's exchange rate against other currencies. The saving-investment imbalance is fundamental, and it alone determines a country's external position.

But the decline in domestic saving is likely to cause the Chinese government to allow the renminbi to appreciate more rapidly. Higher domestic consumer spending would otherwise create inflationary pressures. Allowing the currency to appreciate will help to offset those pressures and restrain price growth.

A stronger renminbi would reduce the import bill, including prices for oil and other production inputs, while making Chinese goods more expensive for foreign buyers and foreign goods more attractive to Chinese consumers. This would cause a shift from exports to production for the domestic market, thereby shrinking the trade surplus, in addition to curbing inflation.

China's trade surplus and the renminbi's exchange rate were high on the list of topics that President Hu Jintao and US President Barack Obama discussed when Hu visited Washington earlier this month.

The United States is eager for China to reduce its surplus and allow its currency to appreciate more rapidly. But they should be careful what they wish for, because a lower surplus and a stronger renminbi imply a day when China is no longer a net buyer of US government bonds. The US should start planning for that day now.

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JOHN SCALES AND LIU ZHI

Will Spring Festival travel get better?

Later this year, just before the fourth Thursday in November, about 45 million Americans will take a break from work and hit the roads, clogging highways, battling airlines and jamming trains. They will make more than 100 million trips; a lot for a country of just 300 million people. They will visit their families to enjoy the comfort of preparing and sharing a traditional Thanksgiving family meal together, followed by watching a game of American football while relaxing in an overstuffed sofa, a cold beer close at hand.

Ask any American and he/she will tell you it is a tradition, a national holiday, and more importantly, it is about spending time with family.

As you read this, in China, another mass movement is underway marking the Spring Festival holiday. An expected 2.8 billion trips will be made before the end of Spring Festival this year. This is on average one roundtrip for every one of China's 1.3 billion citizens. Of course some do not travel during Spring Festival, but most do and a significant number of them make more than two trips. This marks the greatest movement of people in history.

Will travel this year be easier? In some ways it will be worse. Because of China's rapid urbanization the mobile young have moved to cities, leaving parents and grandparents behind. Many others seek temporary employment in cities far away from their families. As with the American Thanksgiving, Spring Festival is traditionally a time of family. As such, over the last 10 years, Spring Festival trips have grown by about 5 percent a year.

But in many ways travel this year will be better. Long gone are the days when most Spring Festival travelers relied on slow over-crowded trains to reach their destination. Over the last two decades, China has launched the largest transport infrastructure building program in the history of the world. Since 1990, nearly 50 percent more railways have been built, 130 percent more roads added and 300 percent more route kilometers opened to domestic air carriers. This additional capacity has significantly reduced congestion, over and above the increase in demand.

Income growth has led to more travelers being able to afford to choose other modes of transport such as better buses, private cars, high-speed trains, and planes. In fact, it may surprise one to note that until recently nearly 90 percent of all Spring Festival travel had been by road, either private cars or buses. But the predominance of road travel is now changing. Travelers are returning to trains for mid-distance trips as new railways with better services open up.

Alternatively, they are choosing to fly for longer distances as air travel becomes accessible to more people. In addition, local governments have established alternate release schedules for students and laborers, thereby spreading the demand for travel over several weeks. The net effect is less overall congestion and better travel quality because travel is distributed across several modes of transport and over a longer period of time.

The good news is that this Spring Festival we are seeing more travel options, more people who can afford to choose, more comfortable and better managed services, and reduced overall travel times.

Could more be done? Yes, of course. Congestion during Spring Festival can be mitigated but not avoided. Building infrastructure is expensive and building for only peak holiday travel is wasteful. No one wants kilometers of underused railways and expressways and airplanes sitting idle during the rest of the year. Better travel comes with a cost which many travelers cannot afford. Ensuring that safe and affordable transport remains available for the poorest should not be forgotten.

The Ministry of Railways is considering changes to its pricing structure that will allow differentiated pricing to distribute demand based on the ability of a traveler to pay, which will, in part, ensure that newly added high-speed trains run at full capacity. But the Ministry of Railways also needs to ensure that cheaper local trains which run on slower tracks are still maintained.

Continued modernization of railway ticketing will reduce corruption and eliminate the black market of overpriced Spring Festival train tickets.

Changes by the government to the *hukou* (house registration) system, together with improving non-farm job opportunities in rural areas, would help bring families together, thus altogether avoiding the need for travel for many families.

Lessons learned from the 2008 winter storm are being adapted by China's transport ministries to help ensure that even if inclement weather hits during Spring Festival, the effects are mitigated. Also where improvement is certainly needed is in transport connectivity; what some call the first and last kilometers, ensuring that getting in and out of railway stations, bus terminals and airports and making transfers is seamless, so that the entire trip is faster and more comfortable.

But we all agree that traveling during holidays, be it Thanksgiving or Spring Festival, will never be easy. The good news is that this Spring Festival we are seeing more travel options, more people who can afford to choose, more comfortable and better managed services, and reduced overall travel times.

And less time spent traveling will mean more time spent with family.

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