Beating the middle-income trap

China should focus on improving living standards and rely less on industrialized countries' development blueprints

By DAN STEINBOCK

According to the World Bank, high-income economies (with per capita gross national income of $12,236 or more) include the United States, Western Europe and Japan, while upper-middle-income economies (per capita gross national income between $3,956 and $12,235) include Turkey, Russia, Brazil and China.

China entered the ranks of the upper-middle-income countries in the early 2010s, and it has great potential to overcome the middle-income trap. First, its unprecedented growth record speaks for itself. Second, the rebalancing of the economy, from exports and investment to consumption and innovation, is proceeding according to the expected trajectory. Third, new growth targets indicate policymakers are well attuned to the need to move from simple growth to higher-quality development. Fourth, deleveraging of local debt has been initiated, which will support sustained growth over time.

At the 19th National Congress of the Communist Party of China in October, General Secretary Xi Jinping emphasized that development is the foundation and key to addressing all problems. China's medium-term policies must cope with these challenges in the "new normal" of the international environment, even as the country's "uneven and inadequate development" is at odds with "people's ever-growing needs for a better life".

Unlike other major economies, China is executing structural reforms, which has proven difficult in other countries. The US is so polarized that some policymakers prefer a government shutdown to a credible, bipartisan medium-term debt-cutting plan. In the eurozone, the sovereign debt crisis has caused huge dislocations and a cyclical recovery alone is not enough to resolve the structural crisis. And in Japan, half a decade of massive monetary injections has not brought about adequate inflation.

In China, economic reforms are central to the rebalancing, which could lift the rest of the impoverished population out of poverty by 2020, just as it is turning the country into the leading actor in global

"If, after two and a half centuries, industrialization is still not complete in peripheral Europe, why is China expected to complete it in three decades?"

efforts to combat climate change through innovation.

To avoid the middle-income trap, the ability to distinguish between appropriate policies and misguided prescriptions is pressing for several reasons.

First, there are the historical lessons. It took advanced economies decades, even centuries, to advance from low-income to high-income economies. Yet many of them demand that today's emerging economies do the same in a matter of years. But when Latin American countries tried to adjust to such prescriptions, they were penalized by "lost decades".

Second, there is the matter of size. Advanced economies like to tout the success of British or US industrialization as a blueprint for emerging countries. Yet when Britain and the US began industrialization, the former had barely 30 million people and the latter about 40 million (the combined population of Shanghai and Guangzhou today). Such laissez-faire doctrines fare particularly poorly in emerging economies, which are larger by magnitudes.

At the regional level, some areas of China's wealthier coastal megacities have already graduated into the high-income category, but the national economy is still in transition. So we should not compare China with industrializing Britain or the US, but ask: How long has it taken for Europe to industrialize, from the first industrial centers in the United Kingdom to rural Romania? In Romania, for instance, more than 25 percent of the people are still employed in agriculture.

If, after two and a half centuries, industrialization is still not complete in peripheral Europe (whose population is only half of the Chinese mainland's), why is China expected to complete it in three decades?

Third, there is the issue of wealth. Advanced economies were pretty prosperous even before they industrialized, thanks not to democracies and free markets but to mainly imperial regimes that grew wealthy on the back of infant-industry protection and protectionism, brutal colonialism, or both. In mid-19th century Britain and the late 19th century US, per capita incomes were at the level that Russia first reached in the 1950s, Brazil around 1960, China in the early 1990s and India just a decade ago.

The trick to overcome the middle-income trap is to avoid those development doctrines that reflect self-interested tenets. The real task is to concentrate on economic development that supports progressive improvements in the living standards of the ordinary people in emerging economies.

The author is a guest fellow at the Shanghai Institutes for International Studies.

Weighing the human factors too

Gross domestic product data alone cannot fully evaluate the quality of China's economic development

By LI YIPING

High-quality economic growth is an important element of Xi Jinping Thought on Socialist Economy with Chinese Characteristics for a New Era. As socialism with Chinese characteristics has stepped into a new era, so has China's economic development, transitioning from high-speed growth to high-quality growth, which in turn will lead to a series of drastic changes including those in the development model and evaluation index.

It is important to remember that there is a difference between economic development and economic growth. The latter refers simply to GDP growth, while the former means all-round economic growth, development and improvement. High-quality economic development thus includes higher product quality and industrial level, and better industrial distribution and product structure.

Scientific, effective and reasonable resource distribution is necessary to build a modern industrial structure and harmonious society, and to make economic development balanced enough to meet "people's ever-growing needs for a better life". In this sense, high-quality development refers to comprehensive improvement in economic, social and natural parameters. High-quality development based on total factor productivity and innovation is what sustainability is all about.

But high-quality development cannot be measured by GDP growth alone. In some cases, pursuing fast-paced GDP growth, the core indicator of economic growth, could be detrimental to quality economic development.

Gross domestic product is an absolute economic quantity concept, first developed by US economist Simon Kuznets in 1934. It is a monetary measure of all final goods and services of a country in a given period (quarterly or yearly) of time. It is especially applicable to economies such as the United States, where all the products are included in transactions.

With the rising polarization between the rich and poor, and worsening environmental pollution, more and more people want a different criterion to be used to measure social and economic development. And some economists have proposed criteria such as "happiness index" and "human development index" as an alternative.

GDP has many shortcomings in terms of evaluating economic development. For instance, it ignores the importance of self-sufficiency. If one woman is employed by a man to do housework, GDP will increase accordingly. But if the man marries a woman and she does the same work as the housemaid, albeit without getting paid for it, GDP will reduce.

Take another example. Sales of air purifiers increase when air pollution levels are very high, which increases GDP but not necessarily people's welfare. Or, when a serious road accident damages a car beyond repair, and its owner, who is seriously injured, decides to buy a new car, GDP will increase, even though the car owner will suffer a loss.

GDP also hides the debt situation, as a region with high GDP may be supported by high debts, which actually carry tremendous financial risks. As such, traditional growth models that yield rapid economic growth may also cause unbalanced, inadequate development, which can hardly satisfy people's high-end demands. And if GDP is considered the main criterion for evaluating officials' political performance, the officials are quite likely to fudge the GDP figures.

Fast-paced, high-volume GDP growth has made China the second-largest economy, but it has also created a lot of problems, including high environmental pollution, serious structural headaches and financial risks. All these suggest GDP should not be used as the main index to evaluate quality economic development.

China's economic development has entered a new era. The transition from high-speed growth to high-quality growth is a difficult but historic process. And global experiences show that achieving high-quality development is much more difficult than high-speed growth.

Therefore, we should first make more efforts to accelerate the transition process and be prudent about economic stimulation. Second, we need to intensify research to determine the best indicator for high-quality development according to the five development principles contained in Xi Jinping Thought on Socialist Economy with Chinese Characteristics for a New Era. And third, we have to create an innovation-friendly environment, in order to improve the quality of economic development.

The author is a professor of economics at Renmin University of China.