

# Important to secure 'sustainable' future

Focus on high-quality growth is correct, says veteran China watcher

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**U**S economist Stephen Roach believes China is right to make high-quality growth its top priority.

Roach, the senior fellow at Yale University's Jackson Institute for Global Affairs and a leading commentator on China's economy, says it is important for the world's second-largest economy to secure a sustainable future.

"Over the past 10 years, the senior Chinese leadership has stressed the need for a more sustainable growth model — namely by shifting from resource-intensive manufacturing to resource-light services. Only then can China enjoy the quality dimension of the growth experience."

Roach, also former Asia chairman and chief economist of investment bank Morgan Stanley, was speaking ahead of China's two sessions annual political meeting, which started in Beijing on March 3.

One of the key focuses of the meeting will be on how to deliver quality economic growth that deals with such issues as industrial overcapacity, excess debt, income inequality and environmental degradation.

Roach says China has already achieved significant rebalancing of its economy, with services rising from 43 percent of the economy in 2007 to 52 percent in 2016.

"China is making good progress toward higher-quality growth. But the journey has just begun," he says.

The 72-year-old veteran China watcher believes Premier Li Keqiang will set a target for GDP growth of around 6.5 percent when he delivers the Government Work Report on March 5.

However, Roach remains concerned about debt, particularly that built up by State-owned enterprises (SOEs), and will be looking out for

announcements in this area in the report. According to the Bank for International Settlements, the corporate sector accounts for 60 percent of the increase in China's debt since the global financial crisis in 2008.

"State-owned enterprise reform will hold the key to deleveraging and reducing the worrisome debt-intensity of the Chinese GDP," he says.

"China's low-return, debt-intensive SOEs have long accounted for a disproportionate share of the increase of total debt in the economy."

Roach has been particularly vocal about the importance of China's growth to the global economy, saying it is now the powerhouse of the world economy, just as the United States was after World War II.

He has calculated that world annual growth would have been just 2.7 percent between 1980 and 2016 — 25 percent less than the actual 3.5 percent — without China's contribution, but stresses the importance of it now moving on to a new growth model.

"The first 30 years of China's economic development miracle were driven disproportionately by a fixation on the quantity dimension. While hyper growth of 10 percent from 1980 to 2010 produced stunning results — a 26-fold increase in dollar-based measures of per capita incomes as well as removing 700 million people from poverty — it was an economic model that placed enormous demands and stresses on the environment."

Roach, also author of *Unbalanced: The Codependency of America and China*, says that moving to the sort of growth model appropriate to meet the 2035 target of becoming a global technology leader, and the mid-century target of becoming a "great modern socialist country," by the 100th anniversary of the founding of the People's Republic of China will not be easy.

"China faces major challenges between now and 2050 that must be addressed as it travels a most daunting road over the next 32 years," he says.

The priority has to be to create a growth model that blends top-down, State-directed policies such as Made in China 2025 with a dynamic private sector, Roach says.

"There has also got to be emphasis on a continued structural rebalancing from exports and investment to consumer-led growth, State-owned enterprise reform and avoiding the middle-income trap by focusing on indigenous innovation," he adds.

"Accomplishing all these objectives, while at the same time focusing on deleveraging and financial stability, is a tall order for any nation, including China."

Roach says the 40th anniversary of reform and opening-up is an important time to reflect on the future direction of policy.

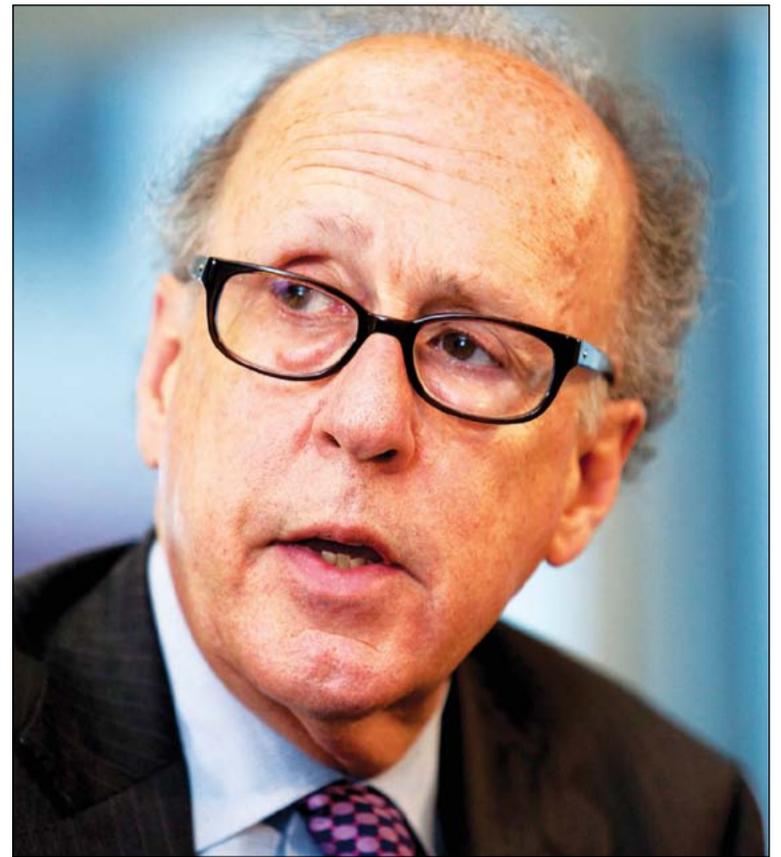
"China is celebrating a very important milestone this year and has much to be proud of in looking back at the extraordinary accomplishments since 1978," he says.

The academic believes that President Xi Jinping was right to suggest, in his report as general secretary to the 19th National Congress of the Communist Party of China, that this milestone could prove to be a springboard to the future.

"Xi implied this milestone should be viewed as more of a pivotal transition point between the economic takeoff of a poor country and the sustained growth of a moderately well-off society that aspires to great power status by 2050," he says.

Roach says it is impossible to play down the role that technology could play in that transition.

A recent European Commission report highlighted that China's leading companies' spending on research and development increased by 18.8



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percent in 2016 — more than double the 7 percent increase of those in the European Union and the 7.2 percent increase of the top US companies.

"There can be no mistaking the increasingly important role that research and development will play in driving the next phase of innovation-led growth in the Chinese economy," he says.

"History shows very clearly that the only way to avoid the dreaded middle-income trap is for a nation to shift its focus from importing foreign technologies to the development of indigenous homegrown ones," he says.

Roach stresses, however, that while research and development investment is necessary, it is not the only contributing factor toward technological advancement.

"Related efforts need to be made in upgrading the Chinese educational system to produce the human capital as well as establishing a Silicon Valley-like startup culture, together with a flourishing venture capital industry. All these are vital in bringing innovation-led growth to the fore in shaping China's new era."

Roach says one of the major challenges for China will be fitting into a world where it is now a dominant player rather than a catching-up developing nation.

"There has to be a daunting reassessment of how China's shifting trajectory fits into the broader world — both from an economic and a geo-strategic perspective."

He says that while China was emerging, its economy was dependent on the rest of the world, particularly for demand for its cheap exports, but now this dynamic has totally shifted, with the rest of the world having a new dependency on China.

"China is now playing an increasingly important role in driving and shaping the rest of the world," he says.

"Fitting the 'next' China into a world that is facing its own set of very challenging problems — ranging from climate change and environmental degradation to mounting inequalities and trade tensions — will undoubtedly present China with enormous challenges in the years to come."

## >> FROM PAGE 4

if the government abandoned targets altogether, letting the economy find its sustainable level, consistent with lowering the debt burden and the growth of new sectors and industries," he says.

The two sessions gathering takes place as China is marking the 40th anniversary of China's reform and opening-up, which led to China opening up to the rest of the world and a transformation of the economy. Zhu at Tsinghua University says it

is important not to regard any transition to high-quality growth as a move away from the principles that were the basis of reform and opening-up.

"I don't think we are approaching a big watershed moment where we are moving to a new growth model. Reform and opening-up was about the market playing an increasingly big role in determining the allocation of resources. I think this path will remain the same. The difference is that the targets are changing fundamentally."

Tse at Gao Feng Advisory believes China is in the process of moving on from its post-reform and opening-up phase.

"China is entering into a new era, and it is one that is epitomized by both confidence and sophistication. It is also one based on knowledge, innovation and a strong will to drive critical global governance and leadership issues as well," he says.

He believes the new era will combine a role for State direction and a burgeoning private sector.

"The top-down central government directive will continue to be strong. There will also be a role for local governments in the middle layer both competing and collaborating to provide further impetus for driving growth."

Kuijs at Oxford Economics believes there are a number of challenges that policymakers will have to face in China's next phase of development.

"The major challenge for China in the coming decades is to work out

whether cementing socialism with Chinese characteristics can be consistent with further opening-up and integration into the global economy," he says.

However, he says the government is aware that the Chinese people will continue to demand a better life and higher standard of living.

"Pushing ahead with reforms to improve China's health, education and social security systems would increase the chance of those demands being met."