China’s Predictable Slowdown

Why the Economists Got It Wrong

Originally published at: https://www.foreignaffairs.com/articles/china/2015-02-18/chinas-predictable-slowdown

February 18, 2015

Salvatore Babones

China might be the world’s largest economy, at least by some estimates, but the growth that got it there is slowing. According to the International Monetary Fund, China's GDP growth in 2014 was less than 7.4 percent, the lowest annual figure since 1980. The IMF predicts that China's growth will continue to slow to just over 6.3 percent by 2019. And even China's usually optimistic central government is expected to lower its sights for 2015 to around seven percent.

The slowdown took almost everyone by surprise. Four years ago, China's economy was growing at 10.5 percent, and the IMF forecast in October 2010 that growth that year would be nearly 9.5 percent, an estimate it confirmed in October 2011. At that time, even the more pessimistic Economist Intelligence Unit had predicted that China's growth would remain above eight percent, at least through 2016. Even so, I argued in the September/October 2011 issue of Foreign Affairs, this growth would merely return China to its historical position as a middle-income country. I pointed out that as China converged toward middle-income status, its growth would slow commensurately.

It was not difficult to see why China's rate of economic growth would eventually decelerate. There are two major reasons, both of which have nothing to do with economics: declining fertility and slowing urbanization. Although a drop in fertility was a boon to economic growth in the 1970s—parents with fewer children could spend more time working—40 years later, that very work force is now retiring and aging parents have too few children to support them.

In fact, a decline in fertility never provides poor countries more than a one-time boost, a benefit that China has now fully realized. The country’s work force started to shrink in 2012, and the trend will continue for decades to come. Even if fertility were to rise tomorrow, it would take decades for those children to reach working age.

Slowing urbanization is also hurting China’s growth rate. In 1980, less than one-fifth of Chinese people lived in urban areas. That figure is now more than half, according to the World Bank. Some experts and officials, including Chinese Premier Li Keqiang, point out that China can still increase the rate of urbanization since it has not yet reached its upper limit. But new construction is slowing, not accelerating; the high—and rising—residential vacancy rates in China's major cities suggest that urbanization is, in fact, reaching its limit.

In short, China’s boom is over. Since 2011, some economists have jumped on the slow-growth bandwagon. In October 2014, economists Lant Pritchett and Larry Summers released a working paper on the subject (although they ignored my arguments in Foreign Affairs).

Indeed, China is not converging to the levels of productivity and economic output found in North America, Europe, and Japan. It is converging to the levels of productivity and economic output found in middle-income countries such as Brazil, Mexico, and Russia. Seen from this perspective, China still has room for growth, but it will be slow and will level out in the 2020s.
As of 2013, China's GDP per capita was still only 64 percent of the world's GDP per capita (83 percent based on purchasing power parity), according to the World Bank. As any casual observer of China will quickly discover, the administrative efficiency of Chinese governments and businesses is much greater than the world average. Pundits may debate China's capacity to someday overtake the United States, but no one who has ever ridden China's high-speed rail network seriously doubts that China will reach the world average.

Although China still has a long and rapid period of growth ahead of it—that is, rapid by anyone's standards but Beijing's—the middle kingdom does not pose a serious threat to the U.S.-dominated world order. China will continue to develop as an increasingly important player in world affairs, but the United States will remain the largest economic and political power of the twenty-first century. American policy pundits would do well to simply calm down when it comes to making predictions about China's growth. Slow and steady progress in China may not make headlines, but it does mean better lives for billions of people—in China, the United States, and presumably the rest of the world.