

Understanding China

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Held annually at the end of March, the Boao Forum for Asia is a grand affair. Conducted in the expansive Boao resort in the province of Hainan, the conference is China's counter to the World Economic Forum in Davos. The Boao Forum has a very different look and feel, an observation that has nothing to do with climate.

Davos leans to the left, Boao has an Asian focus

Unlike Davos, which is Eurocentric, leans to the left and favours government solutions, Boao has an Asian focus and is about trade liberalisation, financial integration and infrastructure. Whereas Davos worries about wellness, inequality, gender gaps and climate change, Boao's accent is on living standards and practical outcomes.

It is clear the Chinese are puzzled by some of our social and economic customs. They see our generous welfare, mandated minimum wage, workplace benefits and high taxes as disincentives to work. They also wonder why our approval processes are so long and inconsistent. Our response that these policies are largely bipartisan isn't very persuasive. It may explain why not much changes politically, but it doesn't address their valid points of high labour costs, declining competitiveness or mixed foreign investment messages.

A bridge too far

Self-interest may lie behind some of the questions from the Chinese. China wants us to employ its workers in the construction phase of Australian projects it invests in. This would provide jobs for its nationals and deliver cheaper assets for its investors, enhancing their returns accordingly. Australians also should benefit from access to lower priced services. But, for any Australian government, the ask is a bridge too far.

Given its communist roots, the contrast between China's emphasis on social and economic policy and policy setting in the West is surreal. While the Chinese are single-minded in their pursuit of personal self-sufficiency and wealth creation, the West is obsessed with state dependence through wealth redistribution, middle-class welfare and capital misallocation.

Listening to Chinese leaders and businesspeople champion the market was music to the ears of Western disciples of Adam Smith. After all, outside of China, they have become an endangered species. But this is modern China.

The Chinese know they must begin a "new magnificent revolution"

The Chinese have had their fill of rent-seekers, crony capitalists, dishonest officials and damaging economic outcomes. They know they must begin a "new magnificent revolution" and move to a more market-driven economy. Anticipating corruption will be a vulnerability. President Xi Jinping has reacted with a crackdown on "tigers and flies" — high-flying and small-time crooked officials.

The genesis of this "revolution" was the November 2013 Third Plenum, which pledged the market and the price mechanism would be the primary determinants of economic decisions and

resource allocation — not the state. The “Reform Manifesto” ruled state-owned enterprises must embrace competition, become more efficient and transparent, and consider mixed ownership.

This manifesto builds on the 1978 reforms of Deng Xiaoping and takes to a new level the application of capitalist techniques to an obsolete centrally planned system. Still, Deng’s “socialist market economy” produced miraculous results. In less than 40 years, 200 million fewer people live in poverty, grain production has increased by 70 per cent and China’s share of world gross domestic product has grown from 1.8 per cent to 6 per cent.

But growth is slowing

But growth is slowing and the leadership wisely decided the system has to be less socialist and more market. Even with social and economic success, the reforms will lead to tension between eroding bureaucratic control and market sovereignty. How the leadership handles this will determine the magnificence or otherwise of the revolution.

China is beset with issues. Its local government and shadow banks are in poor shape. Debt to GDP has grown to Japanese proportions. Wages have soared and eroded competitiveness. There are signs of over-investment, particularly in housing. There are problems with air and water quality. More than 16 per cent of the country’s soil is polluted.

Capital markets urgently need to be opened up so China’s savings pool can be mobilised more efficiently. There is too much reliance on bank credit with, up until now, no bankruptcy laws. This is being remedied. But freeing up financial markets will be a test of the level of confidence the leadership has in the market economy. Beijing has proceeded for decades on the basis of “hide your strength, bide your time”.

Chinese economy has overtaken the US

But when your economy, in purchasing power parity terms, has overtaken the US and is growing at better than 7 per cent annually and your population is 1.3 billion, the time to hide is over. In places as disparate as Sri Lanka and Australia, this reality is seen as a threat, and Chinese investment as potential colonisation. China must recognise this. It has a soft power deficiency and should work sensitively and collaboratively through cultural and other means to allay these fears.

That said, the Australian and Chinese economies are complementary and important to each other. The Chinese respect our governance, natural resources and know-how, we their culture, strategic importance and markets. They acknowledge our Western alliances and geographical location and hope in time to persuade us that “close neighbours are better than distant relatives”. Time will tell.

In the meantime, Boao and Davos will continue to host conferences. They have chosen different paths. One, more than the other, seems to promise tangible hope for the masses.

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