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Analytical study of China's slowdown and its implication on India

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Abstract

China has experienced tragic economic growth in last three decade, and became fastest growing economies of the world and today the second largest economy after taking over Germany and Japan. China's GDP in last three decade has shown increasing trend in double digit averaging near 10%, however recently the China's fourth quarter GDP came to 6.9 percent in 2015 from 7.3 percent in 2014 which is slowest in last 25 years, initially everyone thought it is temporary bubble but in January 2016 GDP reported 6.8 % and IMF forecast it will reduce further moreover stock market crash not only of Shanghai, and Shenzhen but the shares listed in Hon Kong and US of China also declined, China currency declined by 4.4% against dollar, due to such reason it has become matter of concern for the world.

The global economic crises in 2008 greatly affected China's economy as the GDP growth slowed, FDI declined, Export reduced after that year, but the Chinese government responded by implementing a $586 billion economic stimulus package and loosening monetary policies to increase bank lending. Such policies enabled China to effectively cushion the effects of the sharp global fall in demand for Chinese products. However, the Chinese economy has slowed in recent years and projected to be slowdown, The ability of China to maintain a rapidly growing economy in the long run will likely depend largely on the ability of the Chinese government to implement comprehensive economic reforms that more quickly hasten China's transition to a free market economy, rebalance the Chinese economy by making consumer demand, rather than exporting and fixed investment, boosting productivity and innovation, addressing growing income disparities, and enhance environmental protection, as per China official GDP slowdown was expected as China is transiting from manufacturing to service sector and trying to built steadier, stronger economy.

India with demographic dividend and Purchasing power, and large market can be seen as alternate for China by the world, India can't replace China as in comparison China is three fold ahead of India Infrastructure wise, in terms of investment, Foreign exchange reserves and FDI, as per economist the picture may change in long term if India planned and strategically implement policies.

The present paper is an attempt to study the reasons of slowdown of China, historical review of economic growth of China, and how slowdown of China can impact India, the data for the study is limited as the slowdown is recently reported but still the researched has attempted to tap as much data as possible from secondary sources.

Introduction

Three decades ago China was predominantly a rural, poor and closed economy having no connection with the world. The growth and development story of China started from the year 1978 when Deng Xioping took the rein of China after the death of Mao Zedong (the leader of Chinese Communist party, founding father and Chairman of People's republic of China) in 1976, in 1978 several economic reforms are introduced in part starting from agriculture, state reforms and also the open door policy adopted for foreign trade and investment, in 1978 the total volume of foreign trade amounted to 7 percent of its national income, in 1986 it increased to 25 of its national income and by 1998 it reached upto 37 percent of its GDP.

First SEZ established in south eastern Gungdong province for encouraging foreign investment after its success established SEZ in other provinces. It is being mentioned by economist that China followed japan model for development which is export based. China during the reform period realized that for attracting foreign investment there is a need of best infrastructure therefore given top priority to it and developed its roads, rail, electricity and communication. It is being referred by authors that China can built cities overnight but India can't even built roads. Therefore the companies of US and Europe started shifting their manufacturing units in China due to cheap labour and best infrastructure.

At the same time China has done huge investment in real estate and built buildings, skyscrapers considering it to be sold out in advance without registration this all expenditures are done with public deposit in bank and by huge debt taken but because of rise in prices of flats, there are no buyers available for purchasing the costly flats also the stock market of China is least developed and the repercussion of all these is being reflected now as the China's fourth quarter GDP came to 6.9 percent in 2015 from 7.3 percent in 2014 which is slowest in last 25 years. Being the second largest economy of the world it is matter of concern for all economists of the world in starting people think that it was a temporary bubble but not only GDP declined, also stock listed in US and HonKong fall down and also Currency fell against dollar, as per the published opinion of china official it was expected as China is shifting from manufacturing to service sector trying to built steadier, stronger economy, therefore the present study is undertaken to find out the reasons of China' slowdown and its implication on India whether India can benefit or lose out of it

Research Methodology

Objectives of study

1 To study the trend of GDP of China in last 10 years

2. To analyse the reasons of slowdown of China

3. To study the implications of slowdown of China on India

Method of data collection

The research approach of this study is horizontal consist of finance and economics, the research method is analytical and based extensively on secondary data as the topic of research is based on current happenings therefore much research work is not done on this topic but researcher has taken strenuous efforts to get the data therefore, the data for the study is tapped from secondary sources like books, journals, magazines, newspaper, websites.

Limitation

1. Study is limited to time and fund availability
2. The study is limited to implication of slowdown of China on India only
3. The topic of study is current change there are limitation of getting primary data

Result and Discussion

I. Historical review of China's GDP

The economic performance of china in last three decade is impressive, the economic growth story of China started from the year 1978 after taking over of leadership by Deng Xioping after the death of Mao of communist party of China, Deng after visiting several south eastern countries got impressed by their development and introduced several reforms for the development of China and focused more on foreign investment, the economic reforms were carried out in two stages, the first stage in late 1970 and early 1980, involved De collectivization of agriculture sector, opening of country to foreign investment and permission to entrepreneur for starting their own business however most industry remain state owned. The second stage of reforms introduced in late 1980 and 1990 involved privatization of state owned enterprises, lifting of price controls, protectionist policies and regulations, although the state monopolies in banking and petroleum remained. Between 2000 and 2005 the number of state owned enterprises reduced by 48%, reformed banking system, reduced trade barriers and regulation, dismantled much of Mao era social system and joined World Trade Organization. The economic growth of China was tragic during reform era, economist estimate as per literature review China's GDP growth from 1978 to 2013 remained between 9.5% unto 11%. In 2005 replace Japan and became second largest economy after US.

Table 1 Annual percentage of GDP of China

Year	China (%)	India (%)
2000	8.2	5.6
2001	08	4.4
2002	09	4.6
2003	9.6	07
2004	10	08
2005	10.2	8.4
2006	11.2	09
2007	13.2	8.4
2008	09	6.8
2009	6.4	5.2
2010	7.2	5.8
2011	9.4	6.5
2012	9.6	7.1
2013	7.7	5.02
2014	7.5	5.63
Average	9.08	6.50

Source: IMF, World Economic Outlook Database, July 2015

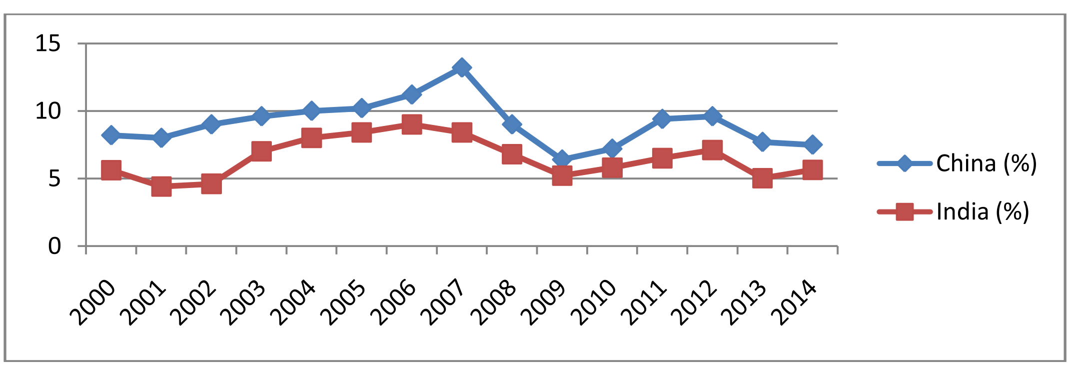

Fig.1 Annual percentage of GDP of China and India

Fig 2 China GDP from 2013 to 2016

From table-1, fig 1 and fig 2 it can be analysed that China's GDP is showing increasing trend from the year 2000 – 2007,GDP is showing increasing trend from 8% to 13%, however from the year 2008-2014 it is showing declining trend from 9% to 7%. The global economic crises of 2008 affected China greatly as China's Export, import, FDI (Foreign Direct Investment) inflows declined and GDP growth slowed, and millions of worker lost their Job, but due to government's stimulus package of $586 billion and loosening monetary policies to increase bank lending helped to recover from sharp decline. However in the year 2015 the GDP came down to 6.9% and in January 6.8% and estimated to come at 6.3% by IMF, not only GDP but recently the Shanghai Stock Exchange Composite index fell by 43%, the renminibi (RMB) depreciated by 4.4 % against dollar. Therefore the ability of China to maintain growing economy in long run depends largely on the ability of government to rebalance it.

While in Case of Indiafrom the year 2000-2006 GDP is showing increasing trend from 5.6 to 9% and after that till 2014 it is declined to 6.5 which is near to China however the average GDP of China is 9% and of India it is 6.5% so even China's economy slowing down India can't match up China or overtake China due to several reasons like week infrastructure, policy, reforms, social structure etc.

II. Reasons of slowdown of China

The initial reaction to the Chinese market meltdown was that it was only a market bubble, but China's not only GDP declined but stock market fall in Shanghai, RMB depreciation and stock listed globally in Hong Kong or in US have also fallen. Following are some of the reasons of slowdown-

1. *The Investment driven model*

During the reform era in 1986 the Chinese government has done tremendous investment in infrastructure, including Road, Rail, electricity, telecommunication and real estate, skyscrapers accounting for almost half of China's output it is said as per literature that the large number of empty unsold houses can be seen in lanes of Shanghais, also it is said that China can built roads overnight. Infrastructure development remained top priority for Chinese government for attracting foreign investment, and for development, the development was so dramatic that a little village called Shenzhen has become in a decade one of world's largest and most prosperous modern cities. The funds for the investment drawn from public money in Banks and on debt, however according to IMF working paper 2012, China's investment have become wasteful and ineffective as there were no buyers available for buying already built houses due to inflation and weak demand abroad. The overinvestment was near about 20% of GDP.

2. *Export led growth*

Post reform period China opened its economy for the world and followed the Japanese model as Japan was export led economy from 1960 to 1970 and japan was the largest economy of that time same way China's export jumped more than tenfold especially during 1990 to 2005 since China joined WTO in 2001 export increased surprisingly by 15% within 5 years. China export rose from $ 14 billion in 1979 to $ 3 trillion in 2014, China's rapidly growing trade flows have made it largest trading partner for 130 countries which includes the list in 2014, 30 countries that makes EU, US, ASEAN countries, South Korea, Japan, Hong Kong, Taiwan etc. China's top three export markets were the United States, the EU28, and Hong Kong, while its top sources for imports were the EU28, ASEAN, and South Korea. According to Chinese data, it maintained large trade surpluses with Hong Kong ($350 billion), the United States ($243 billion), and the EU28 ($127 billion), and reported large trade imbalances with Taiwan ($106 billion) and South Korea ($93 billion). But the world recession of 2008 affected China export in 2009 which was negative, it is being cushioned by China' government stimulus package and pumped funds into the economy due to which it doesn't get affected sharply. But in 2014 the increase is mere of 6% as per review of literature.

3. *Manufacturing sector*

Manufacturing contributes 59% to China GDP, with most of production occurring for export as due to good infrastructure and cheap labour most of US and European Union manufacturing units were transferred to China due to huge reduction in cost, it is being said that everything which is of US or Europe is actually made in China. However due to world economic recession these countries export have slowdown which had a knock on effect on China.

4. *Housing sector and Steel*

The real estate sector account for about 25% & 30% of China's GDP, due to plunging prices of housing, since 2000 residential prices have risen on average nationwide by over 50% despite oversupply in 2007 land prices were rising at annual rate of 15%, which reduced demand not only for housing but also demand of steel, Cement, glass, furniture and appliances. China is the largest producer of steel in the world, it is a major income generator, infact its production is seven times that of second largest producer Japan. However there has been decline in demand for Construction & automobile sector which require steel, if steel prices go down due to overproduction and lack of demand it will have major impact on China.

5. *State owned Enterprises*

Post reform although share of state owned enterprises are reduced but still they continue to dominate number of sectors such as petroleum and mining, banking, transportation, telecommunication etc. are shielded from competition, are the sectors encouraged heavily overseas and dominate listing in China's stock exchange. From study it is found that SOEs constitute 50% of 500 largest manufacturing and service units, in fortune global list of 95 Chinese firm 82 were identified as having 50% or more share of ownership of government

6. *Weak banking sector and increasing national debt*

China' s banking system is largely controlled by Government, and SOEs are believed to receive preferential credit treatment by banks, while private firms are being charged high interest or else have to take credit from elsewhere. As per unanimous source in 2009 SOEs accounted for85% ($ 1.4 trillion) of all bank loan, often SOE's have not repaid bank loans which have saddled large nonperforming asset in banks During the beginning of the global financial slowdown, many Chinese local government entities borrowed extensively to help stimulate local economies, especially by supporting infrastructure projects. In December 2013, the Chinese National Audit Office reported that from the end of 2010 to mid-year 2013, local government debt had increased by 67% to nearly $3 trillion.

A 2015 report by the McKinsey Global Institute (MGI) stated that high debt levels are prevalent throughout the Chinese economy (especially the corporate sector), and that the combined debt of Chinese corporations, government, households, and financial institutions China's total debt rose from $7 trillion in 2007 to $28 trillion by mid-2014. China's debt as of mid-2014 was equivalent to 282% of China's GDP, which was higher than the total U.S. level of 269% of GDP). The report indicated that the rapid increase in China's debt levels was largely caused by real estate and banking loans. Economist believed that China's closed capital account is also responsible for increasing debt as the government has maintained restriction on inflow and outflow of capital for controlling exchange rate of Renminbi, against dollar and other currencies in order to boost export which has impacted financial market.

7. *Underdeveloped financial system*

Despite several economic reforms China 's stock market is relatively underdeveloped due to restriction on market forces. There are two domestic stock market Shanghai and Shenzhen, the main investors are Chinese companies and state agencies, it is controlled by government, foreign investors have limited access to stock exchanges moreover Chinese investors are not officially permitted to buy shares in hong Kong or other foreign exchanges. Both stock exchanges have experienced significant volatility. According to a study by the Brookings Institution, this is largely because the markets are dominated by speculators to a far greater extent than in Western nations, due to speculation Chinese investors purchased shares heavily, being shares investment attractive than bank deposit Chinese stock exchanges are also dominated by individuals (retail investors), who total 200 million and account for an estimated 85% of market trades. Reportedly, more than 30 million new trading accounts were added during the first five months of 2015. Many of these investors reportedly bought stocks on margin (i.e., using borrowed money), betting that stock prices would continue to rise The bubble began to burst in early June. From June 12, 2015, to July 7, 2015, China's two stock indexes fell by 32% and 40%, respectively, resulting in capitalization losses of $3.6 trillion ($1.9 billion and $1.7 trillion), nearly the size of Germany's economy and equivalent to 35% of GDP.

8. *Demographic transition*

At the time of reforms in 1979 China was home to a quarter of people of the world, two third of population was under the age of 30, government felt for economic reforms and for improving living standards there is need to contract population so introduced 'one child policy',. As a result of that birth rate were sharply falling combined with stable, improving life expectancy the proportion of elderly people are increasing In China, the percentage of the population over the age of 65 years was 5 percent in 1982 and now stands at 7.5 percent but is expected to rise to more than 15 percent by 2025. In 2014, working age population reportedly dropped by 3.7 million people, Due to reduction which, the labor charges are raising in China, the supply of cheap labor and younger worker is falling and the foreign investments which were attracted due to cheapest labor in world may shift and impact China's economy.

9. *Environmental Challenges*

China's economic growth model has emphasized on heavy industries development, much of which is energy intensive and highly polluting, also the chemical, and coal pollution increasing air, water pollution, in cities especially several health risk are increasing due to polluted air, So it will require china to shift investment more on health and pension of its people. According to a scientific report, "the air quality of nearly 70 per cent of urban areas does not meet the country's national ambient air quality standards (NAAQS) and nearly 75 per cent of urban residents are regularly exposed to air considered unsuitable for inhabited areas". Based on statistics from China's Ministry of Environmental Protection (MEP), cities in China's Yangtze River Delta, Pearl River Delta, and Beijing-Tianjin-Hebei region suffer over 100 haze days every year, with PM2.5 (particles with an aerodynamic diameter less than 2.5 μm) concentration two to four times above the World Health Organization guidelines. Millions of people in China are breathing a hazardous cocktail of chemicals every day. These chemicals are caused by coal-fired power plants, 27/65 factories and vehicles, and are responsible for heart disease, stroke, respiratory illnesses, birth defects and cancer.

Significantly, most of China's exports are primary goods or manufactured products that create heavy pollution and require intensive resource uses. Chinese factories are still using old technology and many manufacturers lack measures to protect the environment.

III) Implication of China's slowdown on India

From the study it is found that as China and India are less integrated so there will be less impact of China's slowdown on India, however it can have positive impact on India Economist also forecast that things might change in long run as due to one child policy of China, India will take over China in working age population and can create more numbers & skilled workforce,

1. *Trade of India & China*

As in the terms of trade India's Import is more than export from China, China accounts for approximately one-tenth of India's merchandise trade, and bulk of it comes from imports of goods to India. In 2014-15, Chinese imports accounted for 18.4 per cent of India's total merchandise import bill of $448 billion. In comparison, the value of goods exported from India to china was just 3.9 per cent of $310 billion. The trade balance has always been surplus for China since 2002 -2014 while India has deficit in trade balance with India. India Import from China electronic items, telecom instruments, toys, drugs while India export raw cotton, cotton yarn, copper &its articles, minerals, granites and some spices. Due to slowdown in China there will be less demand for raw material and India couldn't get advantage of earning. In case of Import of Chinese goods which is more than imports, India can import at less value can have correction in trade balance?

2. *Manufacturing Hub*

China Slowdown can help in make in India programme, as China is investing in manufacturing and many companies like Hawaii and mobile companies are planned to manufacture in India, many foreign companies are also looking towards India. But still there are challenges of infrastructure, favorable regulation, and taxes

3. *Oil*

From review of literature it is found that, as Oil prices have been reducing from last year to a large part due to slowing global consumption of oil. With demand from China also expected to dry up, oil prices might fall further, which will be more favorable for India which relies completely on imports for oil. Oil is raw material for almost every industry. Therefore, low oil prices mean lower inflation, lower trade deficit and higher production and economic growth.

4. *Automobile*

China was a leading destination for Automobile producers of India With slowing consumption, their demand will fall. It will affect Indian producers

IV Conclusion & Recommendation

China has impressive economic growth in last 30 year post reforms took place from the year 1979, but from fourth quarter of 2015 it has fallen to 6.5 % GDP and still reducing, stock market crashed, currency devaluated which raised concern for the world as China being a second largest economy of the world, export based economy, as a manufacturing hub for many foreign companies can affect to certain extent to the world economies, there are several reason of China slowdown found like overinvestment in infrastructure, real estate with less demand with overburdened debt, week banking and financial market system, export dependent economy as world is facing recession so it impacted China too, moreover, Demographic transition- reducing working age population, increasing elderly, increasing wages, transition from manufacturing to service, but lacking of medium skilled workers, and environmental challenges which divert investment are some of the reason.

Even there is slowdown in China, India can't replace China, because of several reasons China's average GDP is three time higher than India, has substantial foreign exchange reserves of reportedly worth $ 140 billion by the end of 1997, FDI is at level of $70 billion a year compared to India $19 billion. There is a trade surplus of $ 70 billion in 2011 of China while India's trade is in deficit, investment and infrastructure China has investment in several countries of the world and has built an estimated 60000 Km of expressway in less than two decade. Still everything is not rosy in China it has issue of social unrest, absence of human rights, mounting pollution, week Banking system, financial system need revamp, a share of benefit goes to foreign companies which has set up factories in China, week service sector.

India can benefit through slowdown in China is several ways, if planed and strategically dealt. India can improve its trade balance as India's import is more than export from China so India will get benefit of Renminbi devaluation, due to increasing wages of China foreign investment may increase in India, India service sector is more developed than China, India if provide good infrastructure can attract huge FDI, and can increase foreign exchange, India have demographic dividend if utilized effectively in decades to come.

While China is already taking measures for recovering from slowdown like it has devalued it s currency so that it can again increase export, government has offered tax rebates to exporter, banking reforms, stock market control by controlling speculators. Still there is a need of several measure like creating demand inside China, by opening up of interior provinces rural retail sale, improving medium skill, developing service sector, revamping stock market, monetary measures, improving income disparity, enhance environmental protection etc. if China has to maintain long term position

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