China’s prosperity goals and the world

Xi Jinping’s new vision for the economy means less prosperity for people globally

Chinese leader Xi Jinping had set out his vision of “common prosperity” for the people of China at the Central Financial and Economic Affairs Commission (CFEAC) on August 17 this year. However, the full text of his fairly long speech has only now become available in the party journal Qunzhong in its October issue. It enables us to have a better sense of the significant reorientation of economic growth strategy Xi is committed to. This column may be read together with my previous column entitled “Xi Jinping’s Sharp Turn to the Left”, Business Standard, September 13, 2021.

The impending collapse of the Chinese property firm Evergrande should be seen against the background of Xi’s remarks at the CFEAC: “We must improve the housing supply and support systems and insist on the position that housing is for living in and not for speculation.”

He also recommended property tax legislation and reform, something that has been resisted every time it has been brought up.

It was following Xi’s remarks that China introduced new regulations at a stroke, changing the entire policy environment within which the Chinese property and construction sector had developed rapidly over the past two decades and more, constituting nearly 40 per cent of China’s gross domestic product (GDP).

The new regulations introduced the “three red lines”—

- A 70 per cent ceiling on liabilities to assets, excluding advance proceeds from projects sold on contract.
- A 100 per cent cap on net debt to equity.
- A cash to short-term borrowing ratio of at least 1.

None of China’s major property developers are in a position to conform to these new regulations and their inability to do so has meant that fresh financing has dried up. This is something like induced bankruptcy to implement Xi’s directive. Despite risks of collateral damage, there is no sign of a bail out or a more extended deleveraging to avoid disruption. Xi Jinping’s ideological prevarication takes precedence.

Xi’s speech contains other important pointers to what common prosperity will entail in terms of economic policy. For example, he has spelt out the objective of achieving an “olive-shaped distribution structure with a large middle and two small ends.” This will require a progressive taxation regime and greater welfare benefits for those at the lower levels of income. Xi links income inequality in China to global trends. “The rich and the poor in some countries are polarised with the collapse of the middle class. This has led to social disintegration, political polarisation and rampant populism — and indeed the lessons are profound.”

His reading on the social and political impact of economic inequalities is telling and the policies to deal with the latter are likely to be sustained despite collateral diminishing of overall growth.

It is worth noting what Xi has to say about the basic economic system that China must adhere to. “We must base ourselves on the primary stage of socialism and adhere to the two unswerving principles.” One such “unswerving” is to “maintain the public ownership system as the mainstay and simultaneously develop the economics of a variety of ownership systems.”

This confirms that under Xi, it is state-owned enterprises that will form the vanguard of future development not the private sector. The severe penalties imposed on China’s most vibrant and successful private firms such as Alibaba, Weibo and Didi Chuxing and the deliberate bankruptcy of the large private property development companies should be seen as the playing out of Xi Jinping’s ideological preferences.

When Deng Xiaoping was introducing major market-based reforms in the 1980s and encouraging private enterprise through the slogan, “to get rich is glorious”, a more conservative economic planner, Chen Yun, had put forward the view that reforms should expand the size of the cage within which private enterprises should be allowed to operate but the cage of party control should not be dispensed with altogether. Xi is returning to the Chen Yun brand of economics.

This shift in China’s economic strategy will have a significant impact on the global economy. For several years now, China’s economic growth has constituted about 30 per cent of the global economic growth. A slower rate in the coming years, which is inevitable if Xi persists with his new policies, will mean slower growth for the global economy. The latest Chinese quarterly growth figure of 4.9 per cent portends a new trend line. Large production capacities in several sectors in several countries have been built up on this assumption that the China party will continue for many more years. When disappointment sets in and deleveraging becomes inevitable, a lot of companies and those financing them will face painful adjustments. A large number of companies exposed to China prefer not to see the writing on the wall and insist that the slowdown is temporary. It is not. We may expect 4-5 per cent growth as the new normal.

There is a political motivation in the policy shifts we are witnessing. In the years of runaway growth delivered by China’s private sector, a lot of intimate relationships were established between Chinese entrepreneurs and party functionaries at all levels. A symbiotic relationship developed enabling mutual enrichment. David Barboza’s 2012 expose on the wealth amassed by the family of the then Premier Wen Jiabao is well known. And these connections have also been highlighted in the recent book by David Shambaugh entitled Red Roulette. Several members of the so-called “princelings” faction or the descendants of the first generation of Communist revolutionaries fully exploited the opportunities on offer by extending political cover and patronage to comprising business leaders. For example, Wang Qishan is well known for having assisted Jack Ma as the latter built up his Alibaba empire. In targeting these private companies, Xi is also going after their political patrons in the party and ensuring there will be no influential voices resisting the further consolidation of his political authority at the Party Congress next year. Ironically, it was Wang who spearheaded Xi’s anti-corruption drive during his first term as party leader.

What remains to be seen is whether the Chinese economy would be able to tide over the multiple shocks it is being administered. The country has had experienced and pragmatic economic managers who have steered the economy through crises in the past. But this time round their pragmatism is being overridden by ideological preference of the top leader, so unpleasant consequences are possible. A saga that merits careful watching.

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