Getting Prices Wrong - How the state helped China's economic takeoff, 1980-2020

Kent Deng (London School of Economics and Political Science)

Abstract

Deng Xiaoping's reforms began with the concept, 'looking and moving backwards'. The movement represented a renaissance, revitalisation and restoration of the historical market economy and meritocratic schooling that characterised Ming-Qing Chinese. Looking backwards and moving backwards worked. The Maoist straitjacket was shaken off. This was comparable to the Renaissance in late medieval Europe when society went backwards to find solutions for the future. But Deng's reforms went beyond a renaissance by establishing two new goals for China: (1) Higher incomes for households, and (2) greater national strength for China in defence, outputs, and technology (in that order). To accomplish these goals, foreign inputs —capital, technology, and materials— were sine qua non. So, a new era of 'import-oriented industrialisation' began, which has subsequently driven China's exports over the past four decades. External luck also aided China during this timeframe: WTO-cum-globalisation turbocharged China's 'import-export combo' to such a degree that China has now grown to the world's second-largest economy. But an inherent and inborn problem looms for China's 'supply-driven' growth model, working to push the value and volume of China's exports in opposite directions— namely, the more China exports, the cheaper the exports become, collapsing profit margins. As China's cheap exports have ever-increasingly overtaken foreign markets, foreign manufacturing sectors have retreated, accompanied by increased labour unemployment rates and decreased disposable incomes within those countries. Therefore, to continue on its current 'supply-driven' growth model (i.e., to continue selling its exports at scale), China must do so at ever-cheaper prices. The effects of this self-defeating strategy have begun to be seen in weakening industrial output, along with associated strains on employment.