

## Climbing, stretching and stumbling



China's disappointing new growth figures are not the end of the world

ENGINEERS used to dominate Chinese policymaking. But the Communist Party's highest organ, the seven-member standing committee of the Politburo, now includes three economists, for better or worse, including Li Keqiang, the prime minister. On April 14th he chaired his first "symposium" of economists since taking office, inviting views on China's prospects from fellow members of the tribe. The economy, he concluded, would have to "climb hills and cross ridges". Things, in other words, might get bumpy.

One of those bumps was revealed the next day. New figures showed China's economy growing by 7.7% in the year to the first quarter, falling short of expectations and the previous quarter's pace. The figures were puzzling as well as perturbing. The job market still seems tight: there are 1.1 job vacancies for every applicant, the highest ratio since records began in 2001, points out Zhang Zhiwei of Nomura, a bank. Meanwhile, credit seems incredibly loose: the broad flow of financing to China's economy (including bank loans, trust-company loans and corporate-bond sales among other things) set a monthly record in January, then matched it in March.

The links between credit, growth and jobs are not instantaneous. It takes time for disappointing growth to translate into weak employment, because employers hesitate to fire people. Likewise loose credit feeds into fast growth only after a lag (of up to nine months, by some estimates). Since these lags can be long and variable, economists can use them to link almost any unexpected effect with any favourite cause. That is one reason they are held in lower esteem than engineers.

China's uneven figures may also reflect a different kind of cycle: the earth's orbit around the sun. Last year was a leap year, skewing the comparison of this year's shorter first quarter with last year's longer one. If the extra day were taken into account, growth would have been closer to 8%, reckons Tao Wang of UBS, a bank.

The slowdown may also owe something to the new stars in China's political firmament. A frugality campaign championed by the president, Xi Jinping, may have hit conspicuous consumption. According to the National Bureau of Statistics (NBS), the revenues of big restaurants fell (year-on-year) in January and February for the first time since 1978. Tighter

curbs on property speculation, including the revival of a 20% capital-gains tax, have also slowed construction.

#### Quality not quantity

The slower figures may be easier to excuse than to explain. China's new government is intent on "improving the quality and efficiency of growth", according to the NBS. If that is true, it might justify some reduction in the quantity of growth.

More efficient growth would require a lower input of capital (as well as energy and labour) per yuan of extra output. It was, therefore, notable that investment (the addition of capital) contributed only 30% of China's growth in the first quarter. That was an unusually small contribution for an economy often accused of building bridges to nowhere. In 2012, by comparison, investment contributed about half of China's growth; in 2009, more than 87%.

The first quarter's growth was instead led by consumer spending, which contributed over 55% of it, despite Mr Xi's frugality drive. Consumption is often strong in the first quarter, notes Mark Williams of Capital Economics, a research company. But its prominence was no seasonal fluke. In both 2011 and 2012, consumption exceeded investment's contribution to growth—a welcome sign that rebalancing of the economy is finally under way.

These shifts in China's spending mix are mirrored by changes in its mix of production. Services contributed more to GDP than industry for the third quarter in a row. The sector (which includes transport, wholesaling, retailing, finance and property) remains unusually underdeveloped for a country with China's level of prosperity. But this year services may nonetheless become the biggest part of the economy.

That might make the engineers a little wistful. They created an economy in their own image: dedicated to things, not services; durable assets, not consumer trifles. To an economist, by contrast, consumption is, as Adam Smith once put it, "the sole end and purpose of all production". From that point of view, the growth revealed this week was slower but better balanced, and geared towards the consumer. If consumption was not the sole end of the extra production, it was 55% of its purpose. That should be some consolation to the Politburo's economists.

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