

# Conflicts in the U.S.-China Economic Relationship: Opposite Sides of the Same Coin?

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# Objectives

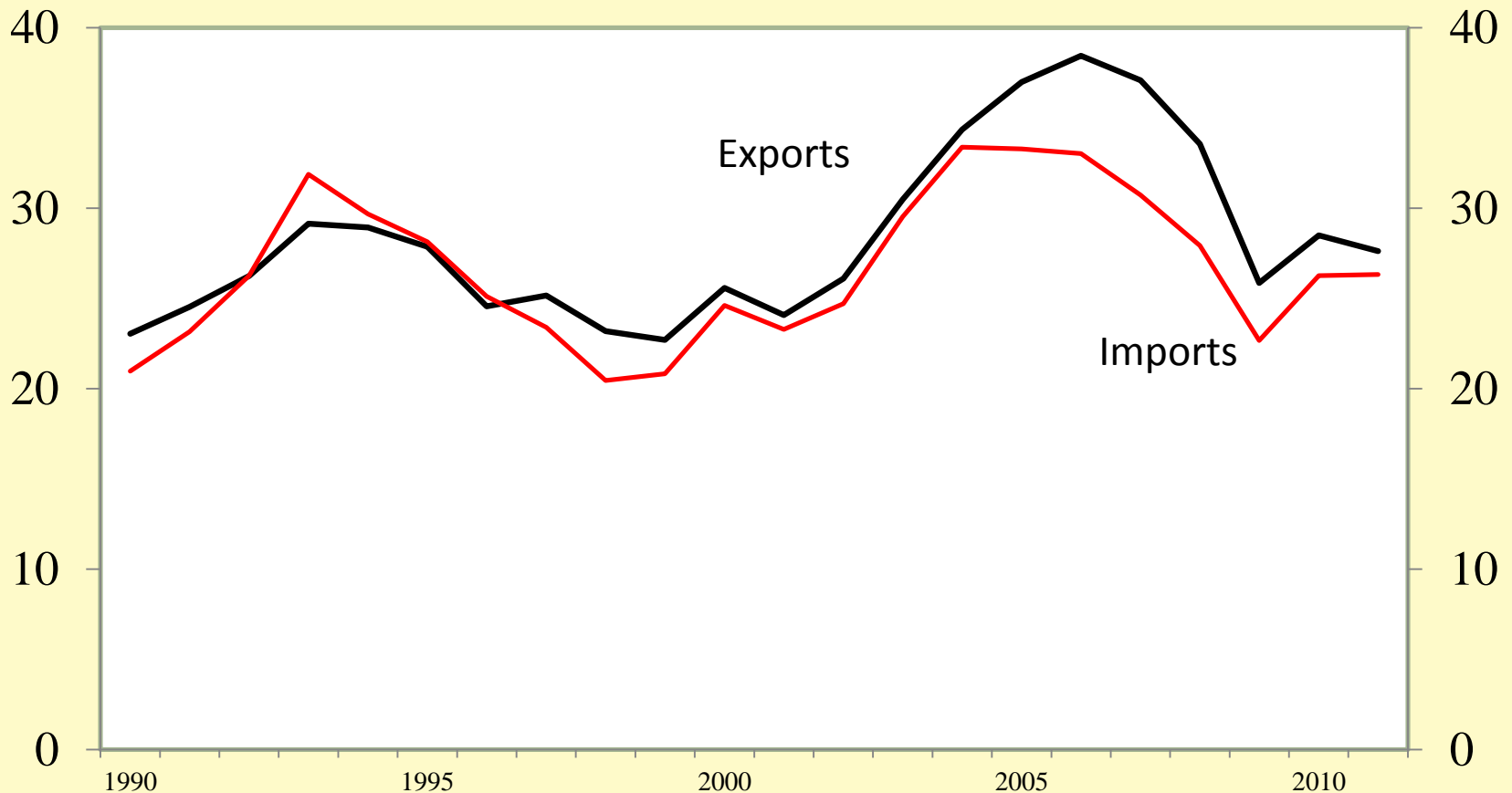
- Rebalancing of Chinese economy
  - Shift of emphasis from export-based growth to development of domestic economy
  - Export driven growth cannot be sustained in future.
  - External changes – trade balance
  - Domestic changes – saving investment
- United States Economic Relationship With China
- Rebalancing of U.S. economy
  - External changes – trade balance
  - Domestic changes – saving investment

# China's Trade

- Distinguish between processing trade and normal trade
  - Processing trade dominated by foreign invested firms
    - Terminal for Asian supply network
    - Relatively low Chinese value added
    - Large trade surplus
  - Normal trade dominated by Chinese firms
    - High Chinese Value added
    - Large trade deficit – sensitive to exchange rate

# All China Merchandise Trade, 1990-2011

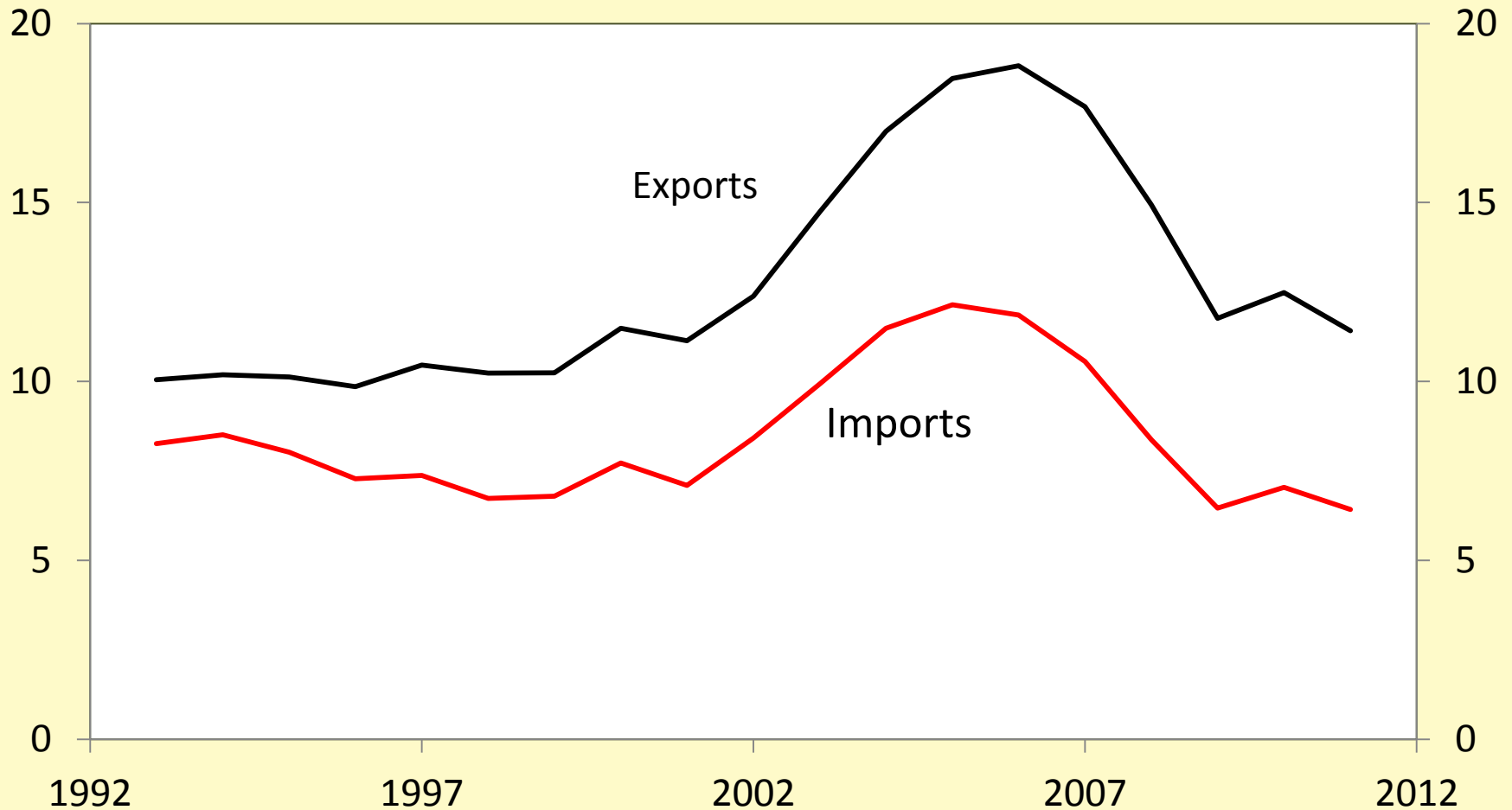
(as percent of GDP)



Source: International Monetary Fund, Direction of Trade Statistics (DOTS), World Bank, World Development Indicators (WDI).

# A. All China Processing Trade, 1993-2011

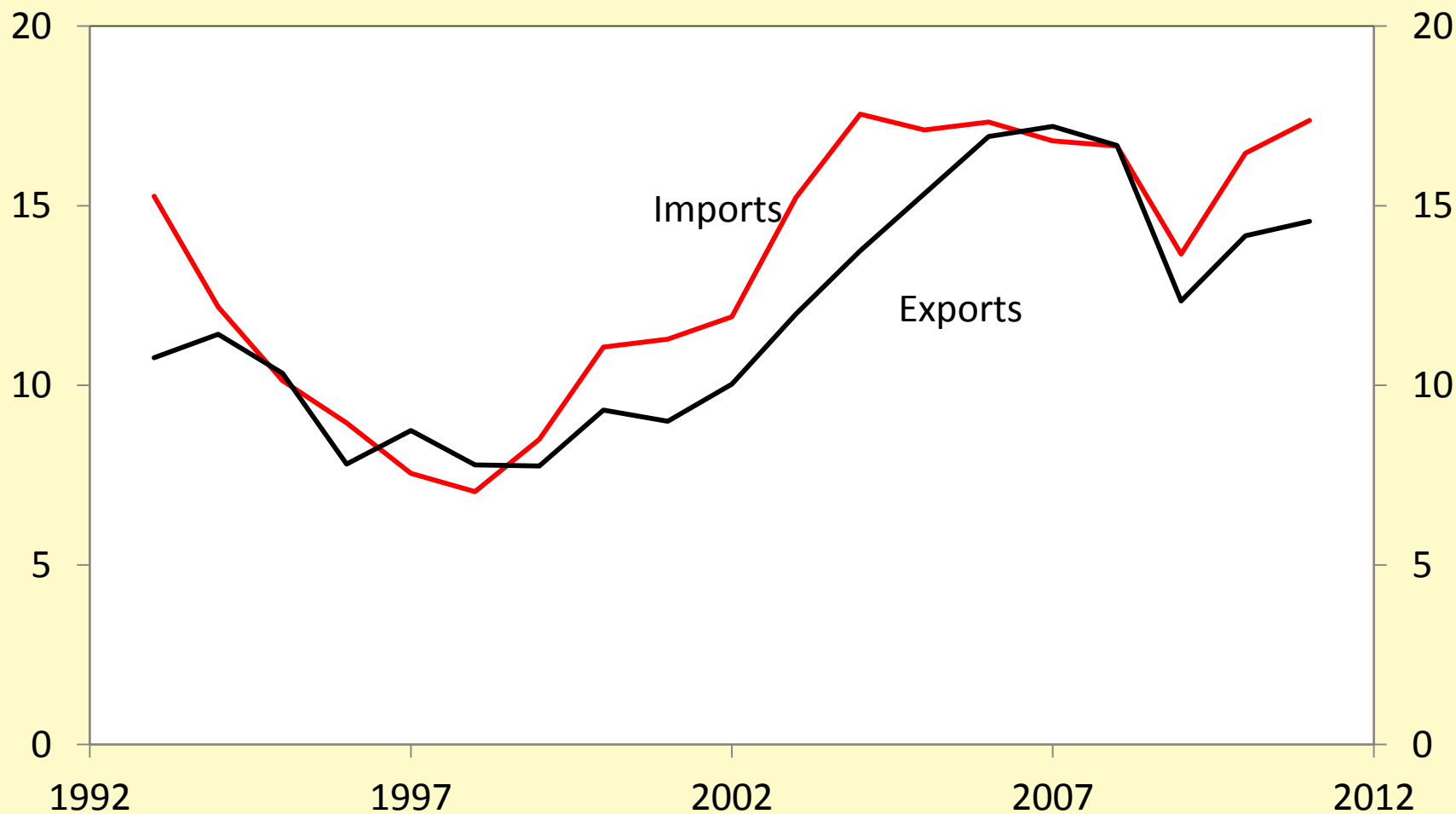
(as percent of GDP)



Source: China Customs

## B. All China Normal Trade, 1993-2011

(as percent of GDP)



Source: China Customs

# Domestic and Foreign Value Added: Normal versus Processing Exports

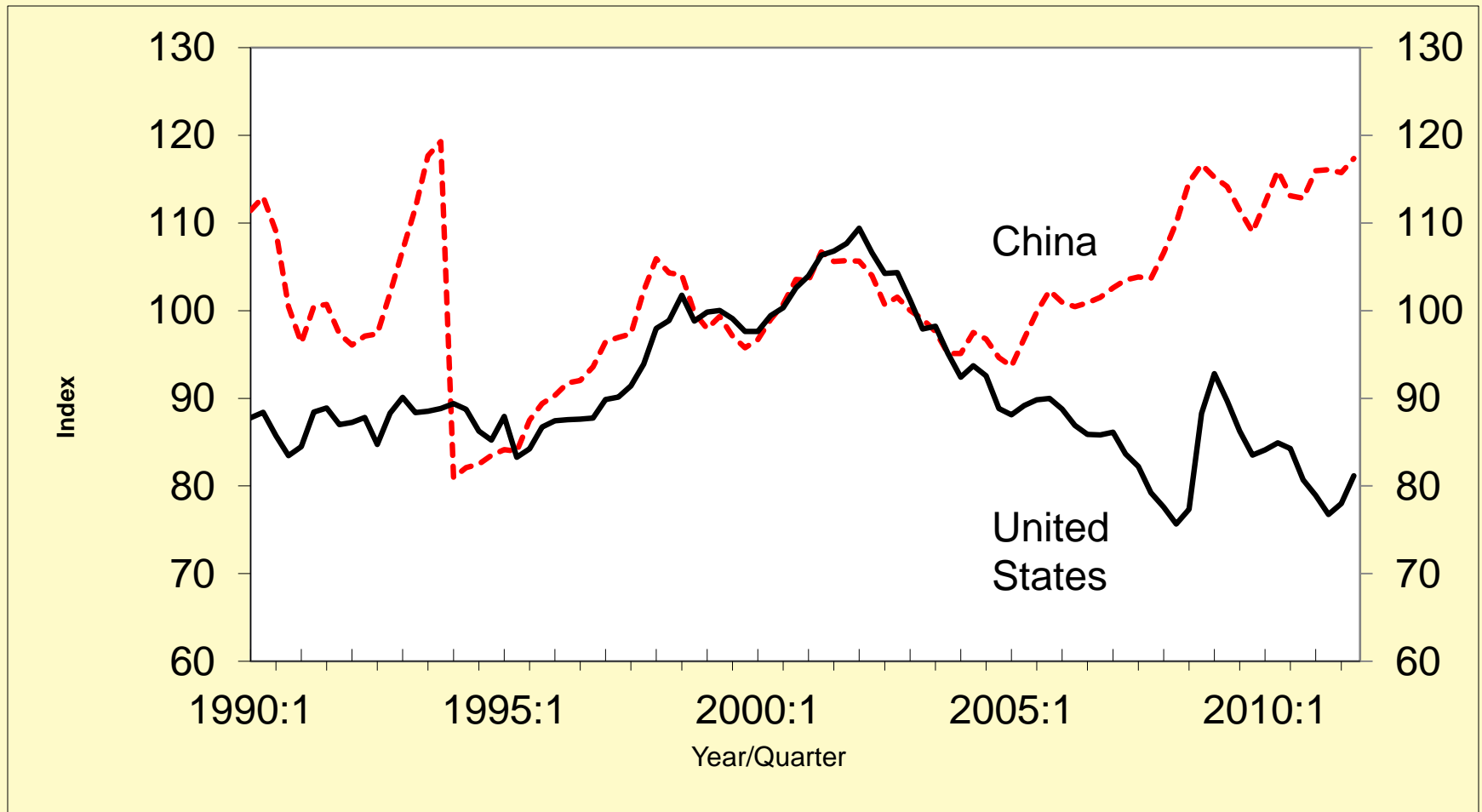
<b>Merchandise Exports</b>	<b>1997</b>	<b>2002</b>	<b>2007</b>
<b>Normal Exports</b>			
Total foreign value-added	5.2	10.4	16.0
Total domestic value-added	94.8	89.6	84.0
<b>Processing Exports</b>			
Total foreign value-added	79.0	74.6	62.7
Total domestic value-added	21.0	25.4	37.3
Source: Koopman, Wang and Wei (2012).			

# China's Exchange Rate

- Importance of a focus on multilateral real rate exchange rate
  - Large appreciation in recent years
  - Major change in competitive balance with the United States
  - But , offset by fall in exchange rates of other major players in Asian supply network.
    - Korea and Taiwan have had major declines in exchange rates



# Trade-Weighted Real Exchange Rate, China and the United States, 1990 – 2012



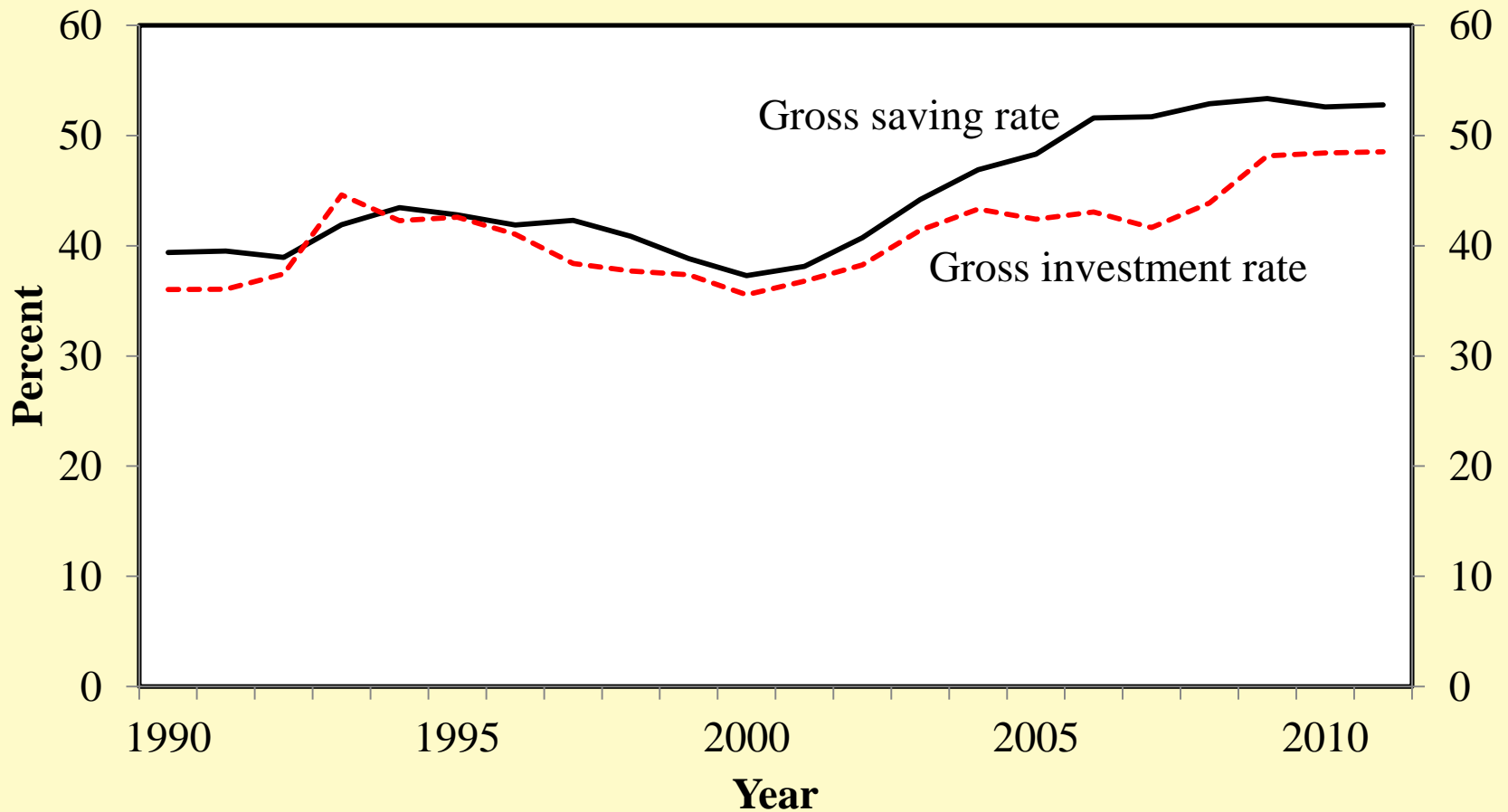
Source: JP Morgan

# Domestic Rebalancing

- Difficult to see evidence of rebalancing on domestic side
  - Narrowing of S-I gap due to continued rise in investment, not consumption
  - Surge of saving in 2000s was widespread: government, corporate, and households
  - Some improvement in household income share in 2009
- Future rise in consumption may be most likely in public sector.

# Gross Saving and Investment, China, 1990 – 2011

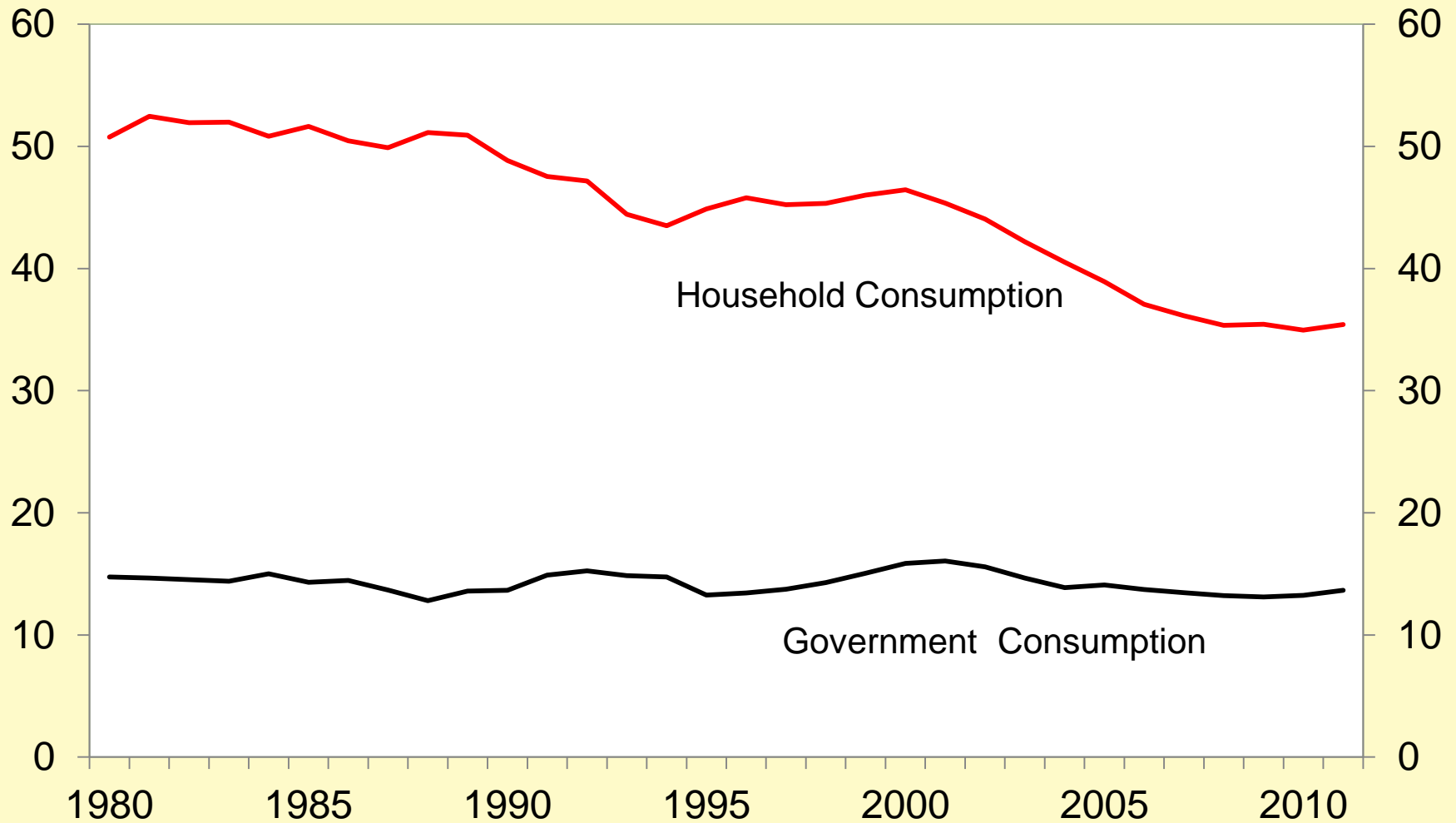
(percent of gross national income)



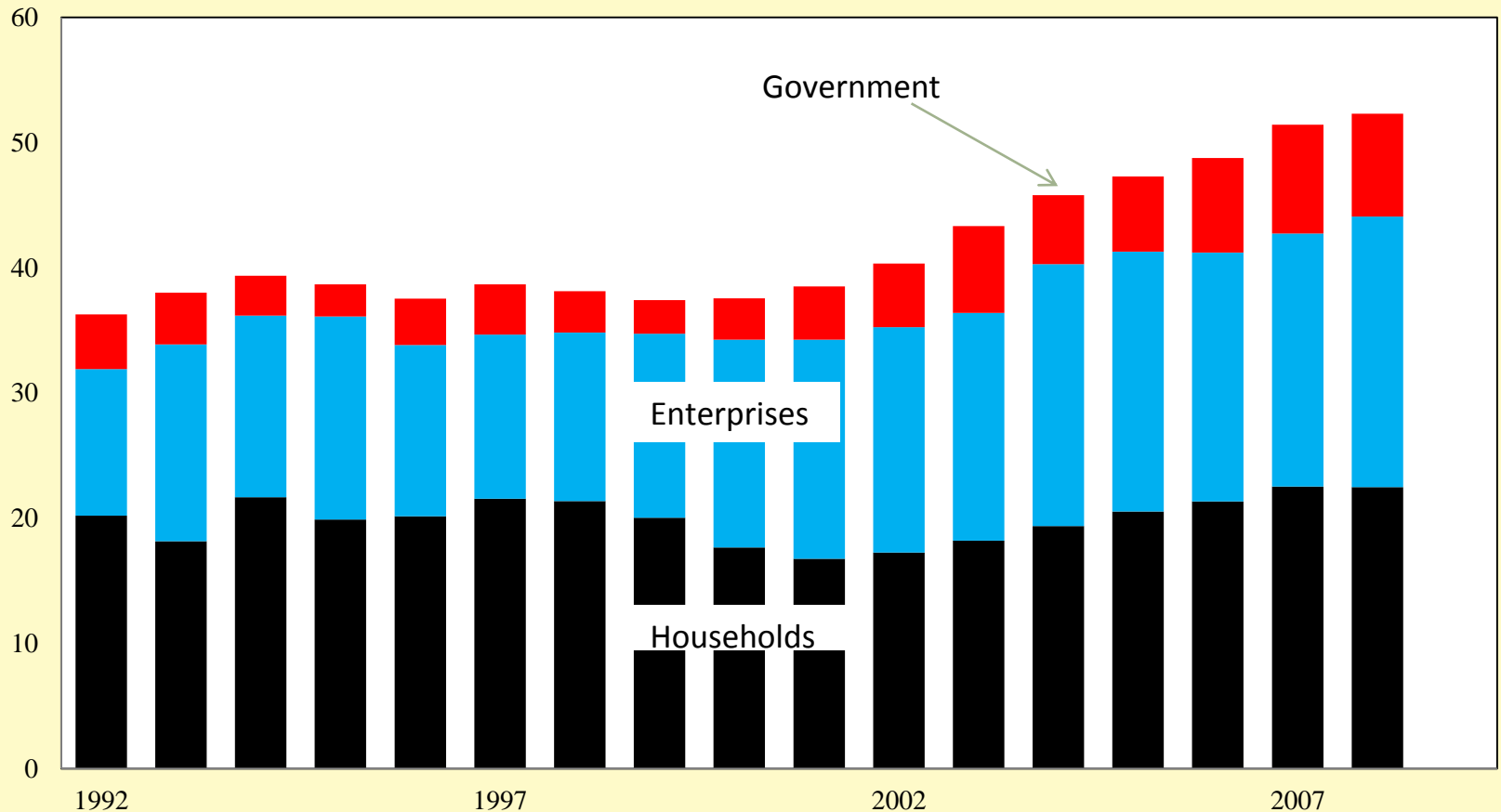
Source: World Bank, *World Development Indicators*.

# Consumption share of GDP, 1980-2011 - China

Percent of GDP



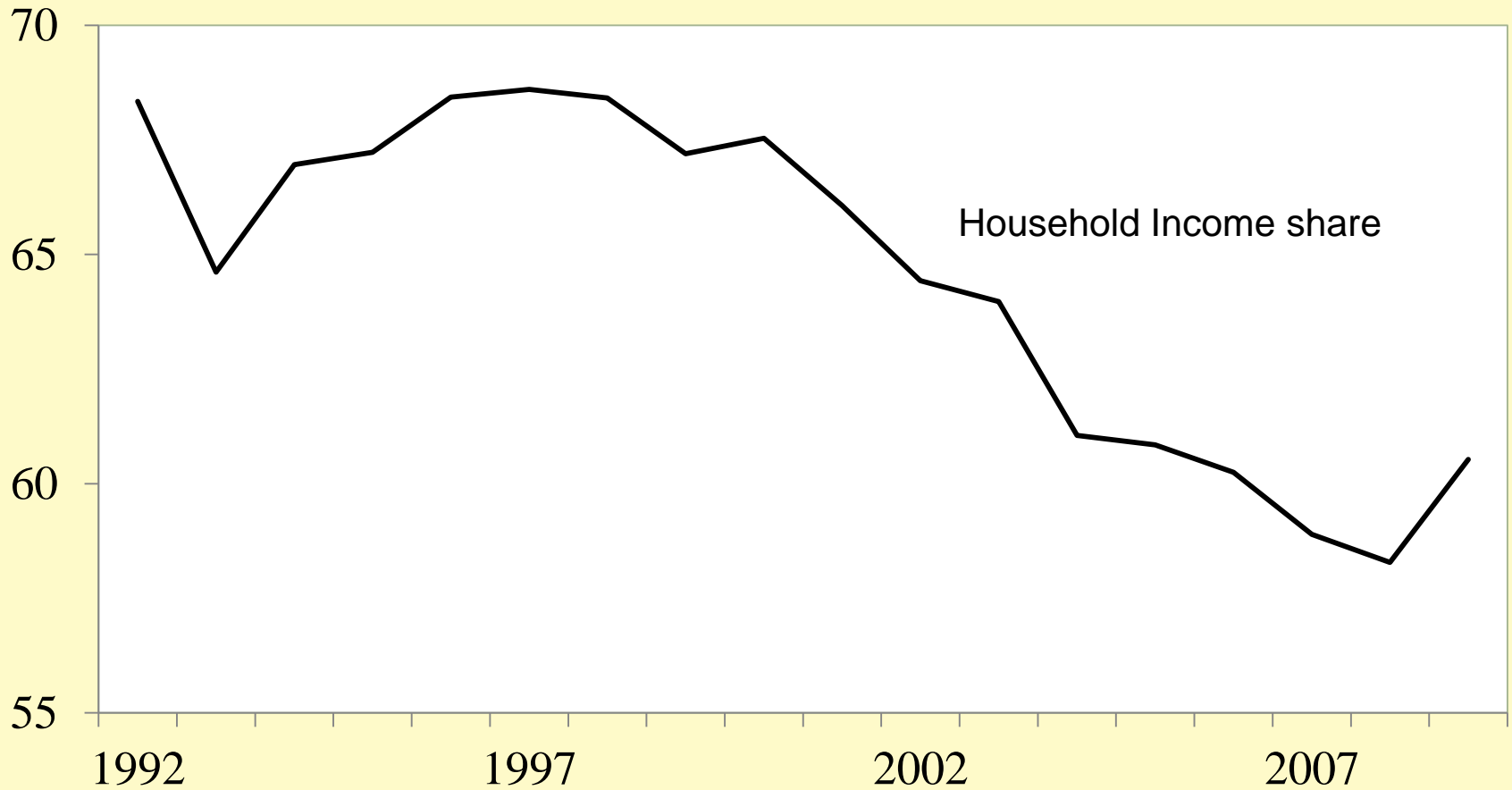
# Gross Saving by Institutional Sector, 1992 – 2009 (percent of national disposable income)



Source: National Bureau of Statistics of China, *China Statistical Yearbook 2012*. There may be a small break in the data series in 2000. The 2012 yearbook reported revisions back to 2000, but they may extend further.

# Household Disposable Income, 1992-2009.

percent of national disposable income.



# United States in China

- Surprisingly low level of U.S. involvement
  - Steady decline in U.S. share of China's imports
    - 2001 – 11.4 percent
    - 2011 – 7.7 percent
  - U.S. FDI in China
    - 3 percent of U.S. global total
    - 15 % rate of return over past 10 years
    - 5-10 % of FDI in China
  - U.S. uses Asian production network rather than its own production facilities

# US – China Economic Relations

- China has reduced its share of exports going to the United States from 29 percent in 2001 to 20 percent in 2001.
- Diversifying toward intra-Asia trade, other developing economies.
- However, China has become a far more dominant source of U.S. current account imbalance
  - 2000-20%; 2005-30%; 2011-67%



# Distribution of U.S. Current Account Balance, 2000-11

(percent of national disposable income)

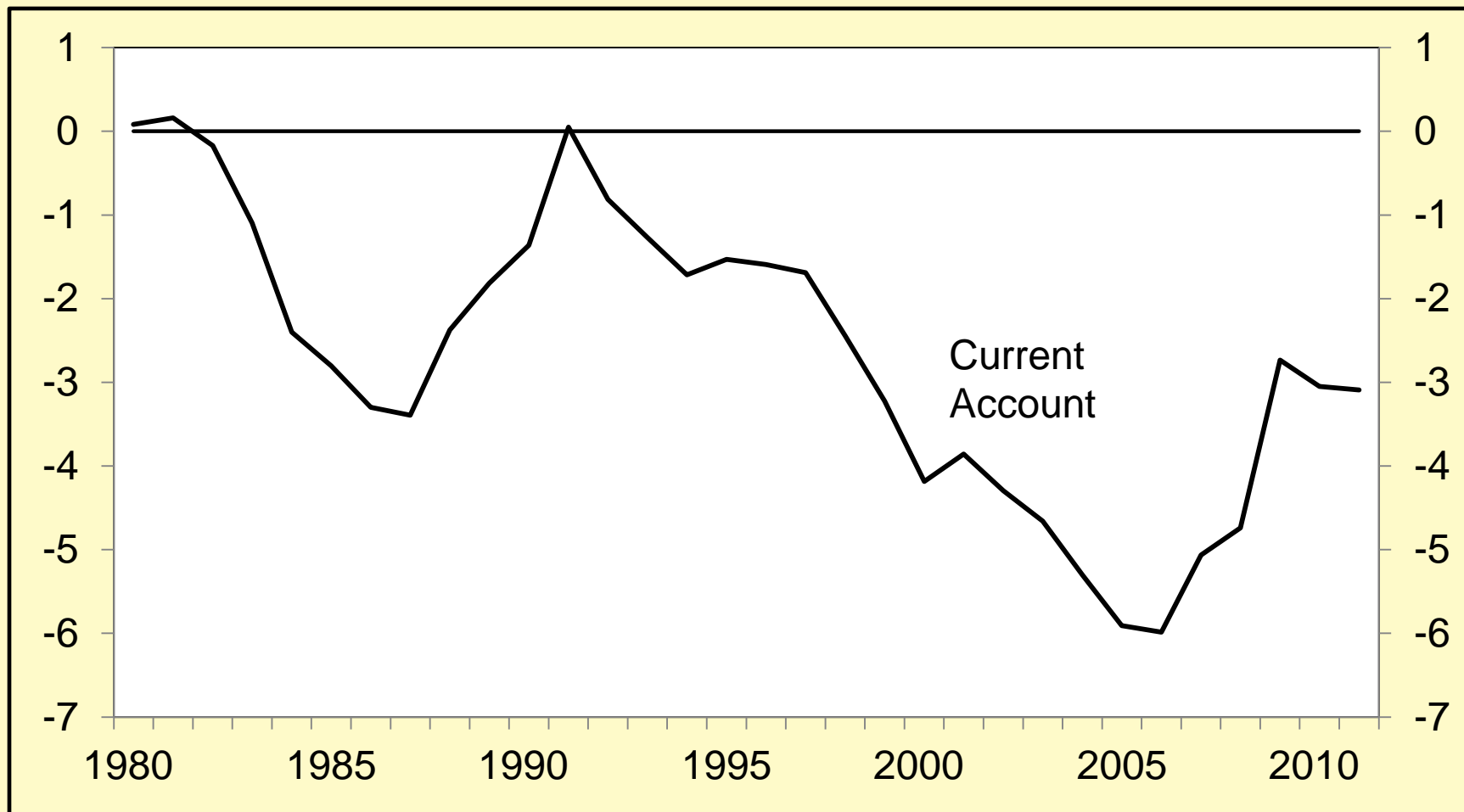
Item	2000	2005	2011	Change 2011-2005
Current Account				
Total	-416	-746	-466	280
Asia	-247	-378	-395	-18
China	-88	-219	-315	-96
Hong Kong	3	9	35	26
Other Asia	-163	-162	-84	78
Canada	-28	-51	27	78
Latin America	-36	-101	16	117
Europe	-74	-127	-13	114
Middle East	-24	-49	-45	4
Africa	-18	-50	-63	-13
Other	11	10	8	-2

# Rebalancing the U.S. Economy

- Opposite of China's situation
  - Large external imbalance
  - Excessive reliance on domestic consumption
  - Low saving and investment
  - Rapid growth of domestic and external debt
- External evidence of rebalancing
  - Substantial decline in current account deficit
  - Sustained fall in exchange rate
  - Continued loss of market share – goods and service

# U.S. External Balance, Flow, 1980-2011

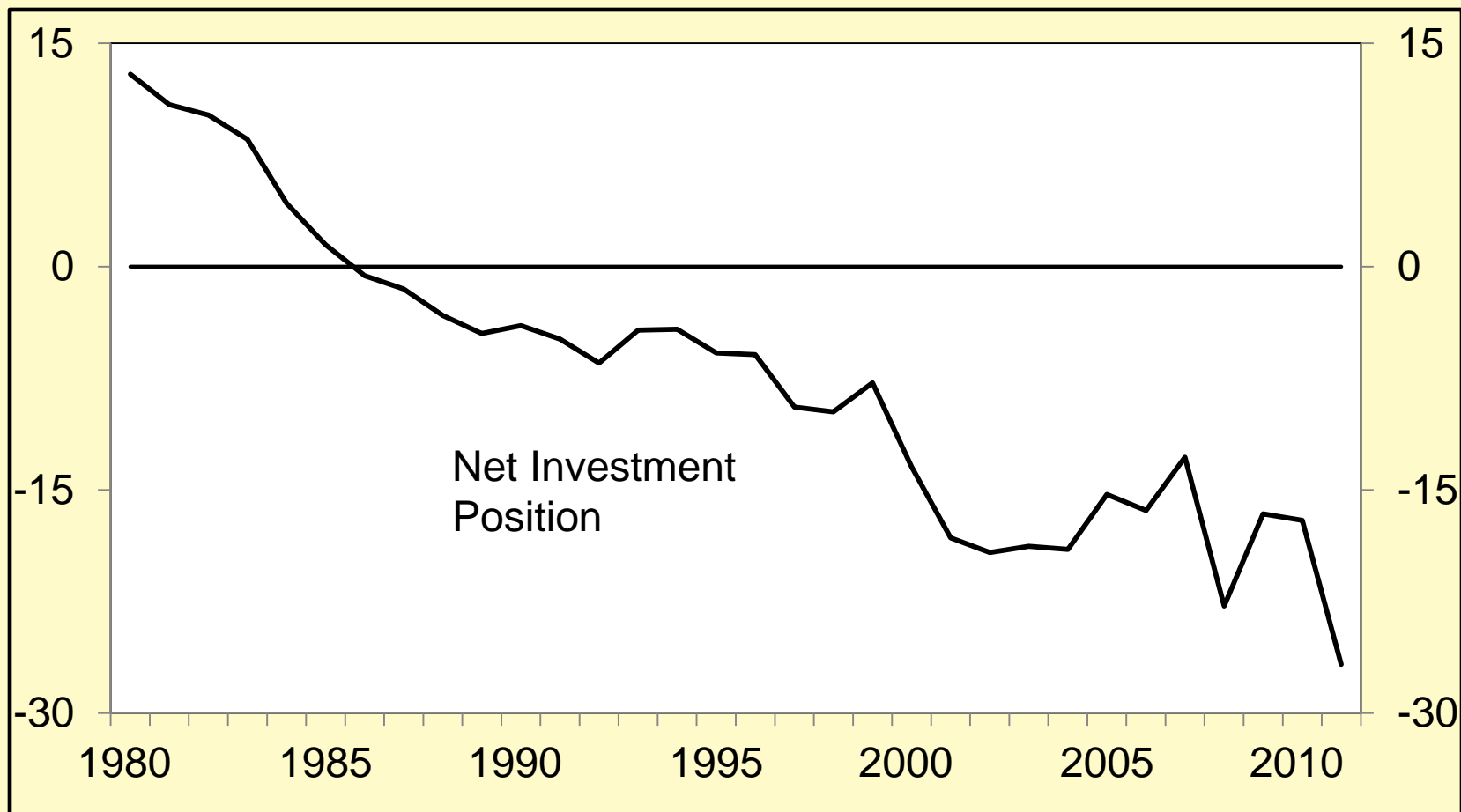
(percent of GDP)



Source: Bureau of Economic Analysis, Balance of Payments and International Investment Position.

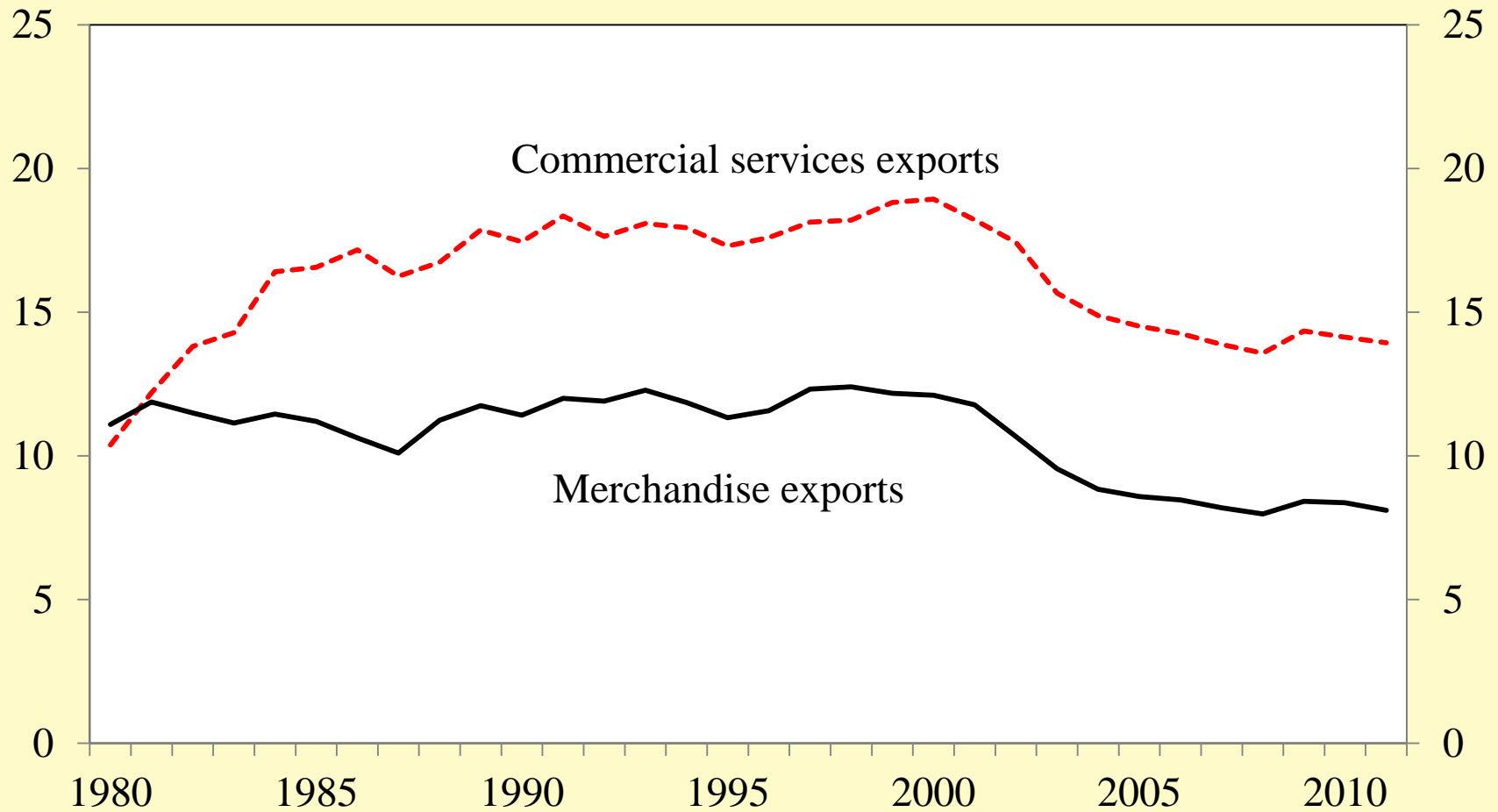
# U.S. Net Foreign Investment, Stock, 1980-2011

(percent of GDP)



Source: Bureau of Economic Analysis, Balance of Payments and International Investment Position.

# U.S. Exports, Merchandise and Commercial Services, 1980-2011 (percent of global total)



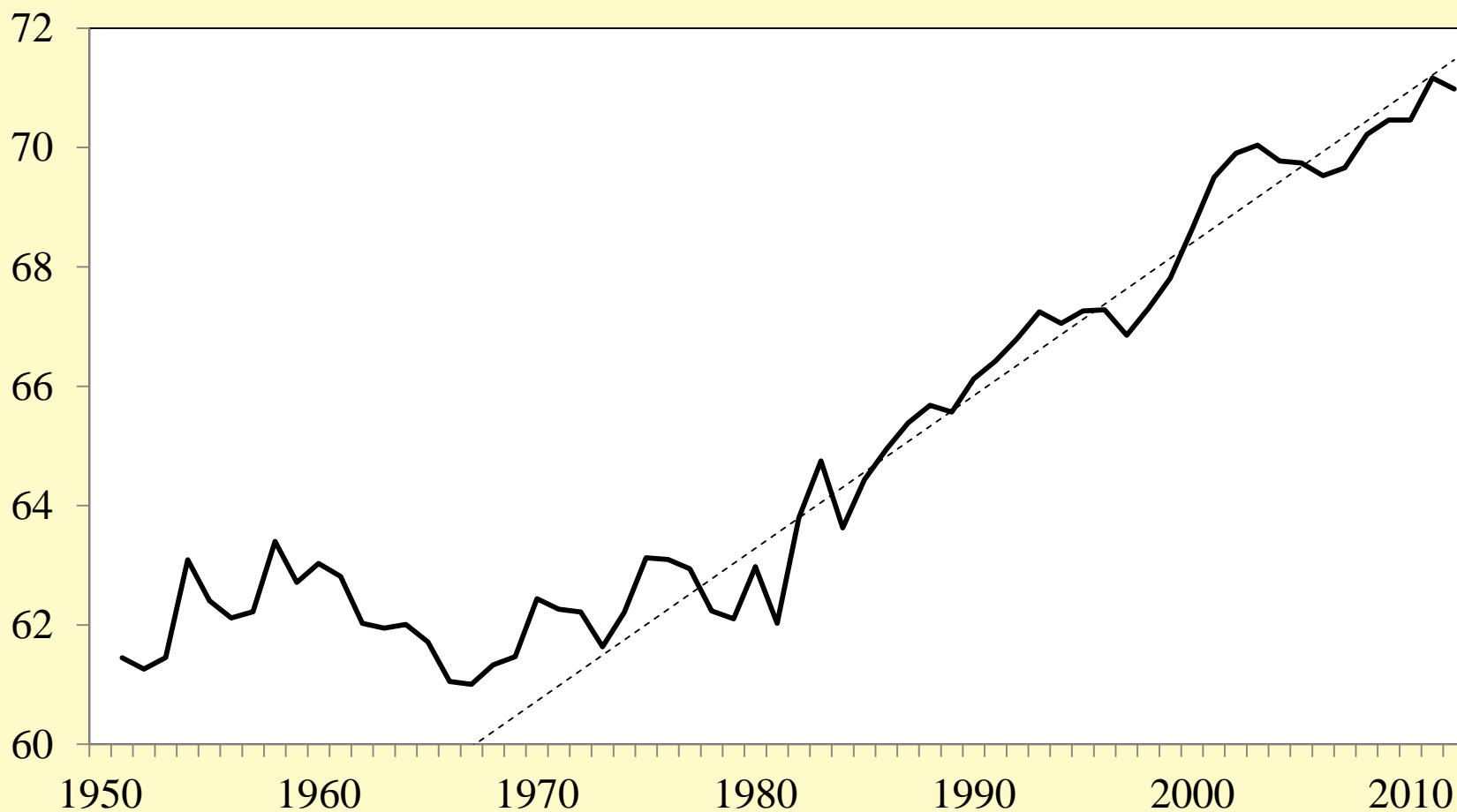
Source: World Trade Organisation, *Statistical Database*

# Rebalancing the U.S. Economy (2)

- Domestic economy
  - Continued surge in consumption share of GDP
  - Household saving rate back to pre-crisis level
  - Negative net national saving rate
  - Very depressed levels of investment
    - Early 2000: 7%      2012: 3%
    - Most of the decline in residential
  - Domestic imbalance → external imbalance ?
  - Ongoing GDP gap  $\approx$  5-6%

# Personal Consumption as Share of GDP, 1951 – 2012

(percent of GDP)



Source: table 1.1.5 of the national accounts and author calculations

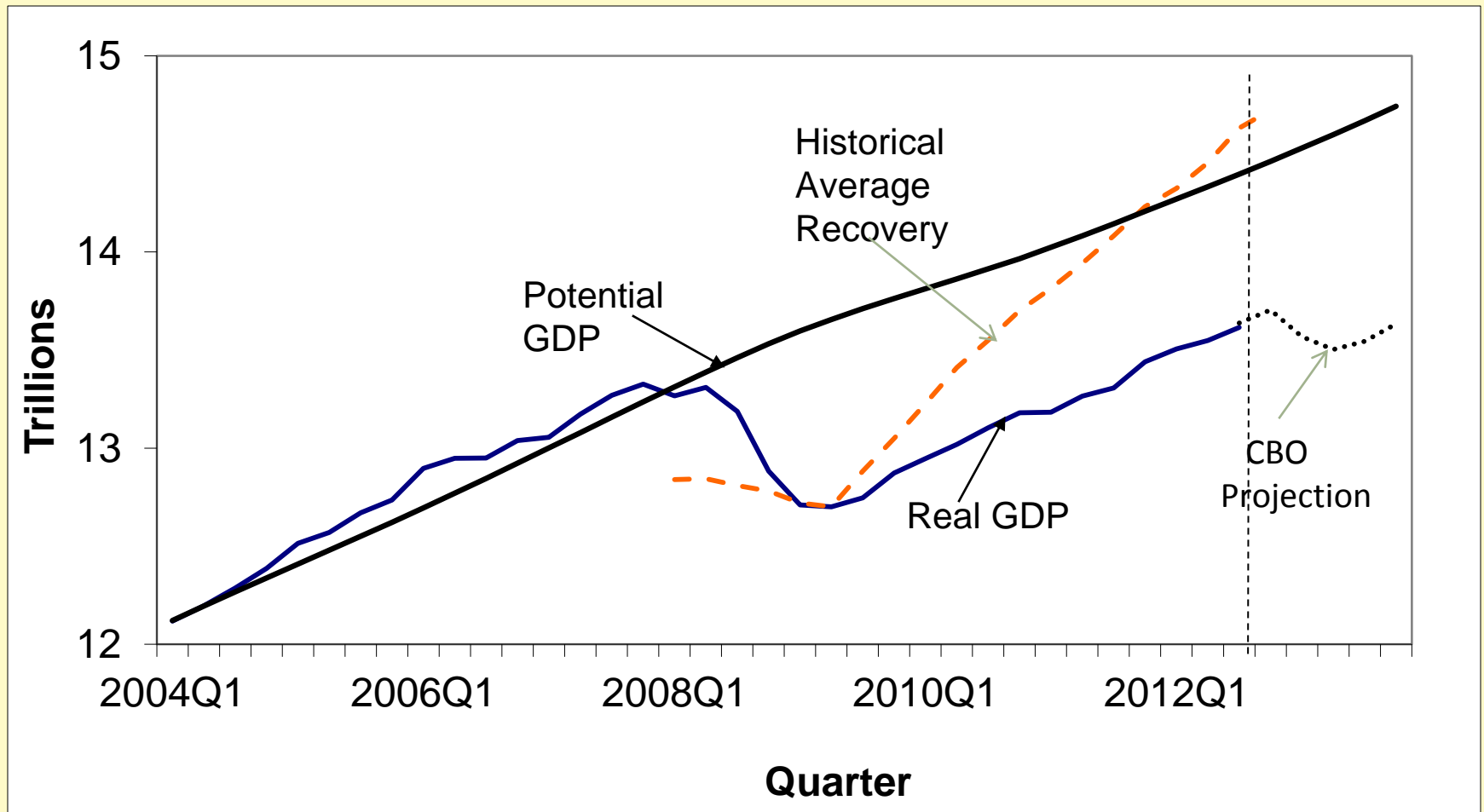
# Components of National Saving, 1960-2012

Item	1960-79	1980-89	1990-99	2000-08	2009-11	2012
Net Saving	10.9	6.3	5.7	3.2	-1.4	-0.2
Government	0.0	-3.5	-2.0	-2.3	-10.7	-8.8
Private	10.9	9.8	7.7	5.5	9.3	8.6
Corporate	3.9	2.9	3.2	2.8	5.2	5.3
Households	7.0	6.9	4.5	2.6	4.1	3.3
Net Domestic Investment	11.2	9.4	8.1	8.1	2.5	3.7
Government	2.1	1.6	1.2	1.3	1.3	0.8
Private	9.2	7.8	6.9	6.7	1.2	2.9
Current Account	0.4	-2.1	-1.8	-5.5	-3.4	-3.8



# Actual and Potential GDP 2004 – 2013

(trillions of dollars)



Source: Congressional Budget Office, Bureau of Economic Analysis, and author's estimates

# Economic Recovery

- Fiscal stimulus versus consolidation
- Problems are structural and not just cyclical imbalances
- Cannot sustain spending in excess of income.
- Recovery will require elimination of current account deficit.
- Improve U.S. as location for economic activity and jobs
  - Lower real exchange rate
  - Increase saving
  - Corporate tax reform
  - Improve labor skills
  - Rebuild physical infrastructure
  - Resolve international standards for intellectual property rights