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The global economy's China headache

To maintain his grip on power, Xi is likely to become more authoritarian. A global trade war is the most likely fallout



Xi Jinping. Hard decisions ▪ REUTERS

As we approach the end of the first quarter of the 21st century, it's interesting to ask which direction is Xi Jinping taking China? China is our most troublesome neighbour.

The answer, whether you agree with the analysis or not, can be found in a NBER working paper, No 32993. It's written by David Y Yang of the department of economics at Harvard.

The news is not good. China will become more politically repressive, resembling what it was like before Deng Xiaoping sort of liberalised it. That is, he went a bit easy on direct Mao type coercion and suppression of liberties.

But the manner of going back to the pre-Deng days, says Yang, will be different. It will be accompanied by unprecedented economic aggression.

He calls the first phase Autocracy 1 and the second phase Autocracy 2. What China is heading for now is Autocracy 3. Same ingredients, differently cooked.

Phase 1 was characterised by Stalinist means of not allowing information flows and very strong bureaucratic control. Phase 2 saw both being relaxed somewhat because the Chinese Communist Party saw that playing with a loose bottom hand would be a better technique under the circumstances.

Changed circumstances

But now the party, or Xi, is moving towards more direct controls over everything because the conditions have changed. The economy is slowing and is no longer able to meet popular expectations. I call it the 'Down, boy' solution, used frequently with teenage sons.

Instead, says Yang, there will be a realignment of incentives, rather in the way, to use my example, we tell teenagers that a new mobile phone will be given only after 99 per cent marks are secured in the final exam. Doable, but only after a very strict compliance with rules that aren't mutually agreed upon but dictated.

As to the bureaucracy, its rewards in terms of promotions will depend on its ability to deliver investment and jobs. This will be critical in determining the eventual outcome.

It's worth remembering that there are two types of Chinese bureaucrats: administrative and political. It's the latter that matters to the politburo. The former are just the worker ants.

Yang's remarks about the leaders of an autocracy are of interest to us as well, not because we are an autocracy but because of what he has to say about leaders who promise things to voters and the party people. He says, along with other academics, that the key to continuing leadership lies in the credibility of the promises being made.

According to him this is the central problem facing Xi now that the economy has begun to slide. If people stop believing him and therefore the CCP, greater repression will follow in what he calls Autocracy 3. Curiously, he hasn't considered the usual solution that political parties adopt: changing the leader.

I should add my own two-bits by asking if the rest of the world should be worried. That depends on the extent to which the CCP and Xi decide to ratchet up their export production in order to maintain and increase employment in China.

We are already seeing the beginning of aggressive export policies. Recently it also cut its interest rate suggesting that it isn't not worried about inflation — after all, wages can be kept down forcibly.

The only option the rest of the world will then have is to increase tariffs against imports from China. This has also begun happening. Net-net, an all out trade war seems inevitable because the CCP wants a monopoly on power.