# Chinese Capital Flight

China's economic development is a fascinating case study into economic phenomena on many fronts. Its unique history has created an economy that is simultaneously an accelerated analogue of and an antithesis to the Western world's economic development. Perhaps the single most important variable that has affected the Chinese economy over time is the degree to which its economy is isolated from the rest of the world. The Chinese Communist Party (CCP) today finds itself in a difficult position where its past decades of remarkable growth were driven by an embrace of the capitalism and globalization, but its past several millennia of cultural history were defined by isolationism. One challenge facing the CCP, capital flight, most effectively demonstrates China's struggle with the free market and tests the integrity of China's elite. More accurately, China is not in the midst of a panic with investors trying to export money as quickly as possible, rather, China's wealthy class is slowly transferring their wealth out of the Chinese economy, further contributing to already high inequality. Like in most other cases of capital flight, China's is motivated by distrust of central institutions, but the bigger problem is how this distrust is so deeply rooted in the workings of the Chinese government.

Firstly, why has capital outflow become such a major problem in China? The single most important reason is also the most obvious: There is little faith in the long-term stability of Chinese investments, largely due to the high degree of autonomy with which the CCP governs its economy. To be clear, there is little evidence on which to claim that the CCP's rule is at risk of overthrow, rather, the CCP's very manner of ruling the nation is the cause for investors' anxiety. Just recently, the CCP suspended fintech firm Ant Group's initial public offering on the Shanghai and Hong Kong Stock Exchanges, the expected to raise a record USD $34 billion; the company itself was valued around $310 billion before the IPO's suspension. Arguments can be made over the true motivations behind this decision, whether Chinese regulators sought to protect the Chinese economy from a high-tech bubble or if paramount leader Xi Jinping simply wanted to spite billionaire Jack Ma. Regardless, the move is a stark reminder to investors globally that the Chinese government can and will take drastic action regarding their economy and does not need to offer any justification to its non-existent electorate.

In addition to such examples of intervention from a central government, other remnants of the People's Republic of China's anti-capitalist formation can be seen. The Chinese real estate market has been growing immensely in recent years thanks to a growing upper class. Many Chinese cities now face the same affordability crises as Western cities, whose own unaffordable housing is at least partially at the fault of these same Chinese elite. Lurking over all real estate transactions in China though is the threat of the 70-year lease. The Chinese government nationalized all urban land in 1982 and began leasing it out on 70-year contracts in the 1990s (some contracts were much shorter). To prevent panic in the real estate market, the Chinese government has so far renewed at no cost all of the shorter contracts that have already expired, but there is still little assurance as to what will happen decades in the future when the bulk of these contracts begin to expire. Will the CCP charge a fee for renewal, take back the property outright, end the temporary leases, or will they kick the can down the road another several decades? Keep in mind that China currently has no property tax and lawmakers seem timid about approaching that as a potential alternative to state ownership, for reasons we shall see shortly. Overall, it's easy to forget that China's current government was formed only in 1949 and has, in just seven decades since, witnessed both immense catastrophe and sweeping reform, the recent decades of stability have been brought about only by the capitalist reforms of the 1980s. In short, Chinese investors have good reason to be anxious.

So, this explains the general paranoia among Chinese investors, but who exactly are these investors and in what ways are they driving capital out of China? Herein lies the dilemma facing the Chinese government, most of those in positions of power to affect economic policy are part of the very Chinese elite with the capital and the means to move said capital out of the country. To clarify, CCP officials make up an extremely small fraction of China's nouveau-riche (which is itself a very small fraction of the general population). In general, most rich Chinese people aren't Chinese lawmakers, but most, if not all, Chinese lawmakers are rich Chinese people. Why would Chinese officials introduce a property tax when they are personally the owners of multiple homes? Why would they want to restrict capital outflow when they need to wire their children tens of thousands annually to pay for their tuition in North American, Australian, and European schools? Not to mention the amount one must move to buy foreign homes.

This conflict of interest paired with lack of accountability to the public certainly make lawmakers reluctant to impose permanent solutions and make drastic changes, but that's not to say that the problem has gone entirely unaddressed. The problem has been addressed quite directly, albeit quite ineffectively. Chinese citizens are now subject to an annual limit of USD $50000 per person in capital transferred to foreign nations. Notably, luxury homes and international tuition can often cost a lot more than the limit allows. Hence, the rich must circumvent this limit, legally of course. Typically, one can transfer the maximum amount every year over the course of several years, multiplied by some number of cooperative relatives and acquaintances (recall that the limit applies *per person*). In the grander cases, in which the amount of capital being moved is several orders of magnitude too large, there are always legal loopholes to take advantage of. It seems, then, that such measures are more of a nuisance to the rich than they are effective at keeping money in the Chinese economy, and their inefficacy is fully intentional. Moreover, these measures against capital flight are part of a greater narrative describing the CCP's unconventional means of creating the image of a growing economy in the wake of the historically rapid growth of the late twentieth century. Other activities include increasing accessibility of Chinese stocks to foreign investors and intentionally devaluing of the Yuan/RMB against the US Dollar, also in attempts to attract foreign investment.

A more superficial reason for capital outflow has to do with a perceived superiority of foreign products. Foreign education and housing are highly desirable to those who can afford it. Whereas plenty of wealthy Chinese are buying foreign homes and sending their children to foreign schools, the wealthy classes of other nations are not as eagerly buying Chinese real estate and investing in Chinese education. The most obvious partial solution is already being implemented, the domestic quality of higher education and luxury real estate is catching up quickly, but the more fundamental problems cannot be solved so easily. Exacerbated by the current cultural dynamic between China and the West, the fundamental problem is still in the Chinese government's self-imposed untrustworthiness.

There is frequent disagreement as to whether today's People's Republic of China ought to be considered capitalist or communist. Ultimately, the notion that communism is the antithesis of capital is mislead and rooted in silly Cold War ideals. To describe it more accurately, China has no shortage of capital and the various capitalist entities that naturally arise when allowed to; yet the government insists on maintaining a great degree of control, control which it is not shy to remind us of. On the understanding that capitalism is defined by a lack of centralized control of the economy, then China is not as capitalist as the United States. Although, China is just as capitalist as the United States in the more derogatory, anti-American sense of the word.

In many ways, the CCP's attempts at maintaining a stable economy is itself a major threat to this stability. The Chinese government is fundamentally at odds with itself, initially founded on a dream of true communism, presently run by individuals who benefit greatly from the exploits of the free-market, and ultimately unwilling to surrender control to this invisible hand. Investors, however, invest on the expectation of some, usually positive, outcome. In a nation where that outcome is at the whims of an opaque authoritarian bureaucracy, investors have good reason to be wary. And this bureaucracy's attempts at forcibly eliminating this anxiety are unsurprisingly counterproductive. To follow the precedent of the more stable economies elsewhere on the globe, China should increase transparency, reduce personal restrictions, and intervene in the market for the protection of consumers rather than politicians. China needs to build trust, not enforce it, but then again, when has this China ever followed precedent?

Works Cited


https://www.scmp.com/economy/china-economy/article/3098814/china-stuck-rigid-controls-capital-outflows-becoming-harder

https://www.washingtonpost.com/opinions/2020/11/11/chinese-communist-party-just-showed-jack-ma-rest-us-whos-boss/

https://www.cnbc.com/2020/11/10/ant-group-valuation-could-be-cut-by-over-150-billion-after-halted-ipo.html

https://www.scmp.com/comment/opinion/article/3109261/delay-ant-ipo-small-price-pay-getting-new-rules-right

https://www.forbes.com/sites/sarahsu/2017/03/21/good-news-for-chinese-homeowners-premier-li-offers-some-clarity-on-land-leases/?sh=7646b1177b4a

https://asia.nikkei.com/Business/Markets/Currencies/China-clamps-down-on-capital-flight-risk-as-yuan-weakens

https://www.scmp.com/economy/china-economy/article/3040629/us-dollar-transfers-cut-back-chinese-bank-beijing-steps