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Study Shows Trade's Shrinking Role in China's Growth

By BOB DAVIS

BEIJING—China doesn't depend much on its trade surplus for growth any longer, according to a World Bank study, marking a sharp shift in the development model that helped turn China from an economic backwater into the world's second-largest economy.

While China's trade surpluses are expected to average around $200 billion in 2011 and 2012, the World Bank said, that is 2.7% of projected gross domestic product, or just 0.2 percentage point of its expected growth.

Part of the reason for the diminished role for trade in China is meager demand in the rest of the world, which is struggling to recover from the global financial crisis, said Louis Kuijs, a World Bank senior economist in Beijing. But he also pointed to "a structural process going on, coming from a strongly growing Chinese economy" that sucks in imports.

The World Bank study could make it more difficult for the U.S. to argue for further Chinese action on its currency, especially coming on the heels of a quarter in which China ran a small trade deficit.

U.S. political leaders for years have pointed to China's immense trade surpluses as evidence its currency is undervalued, and have pressed Beijing over and over to increase the yuan's value. The two countries are bound to tangle again over China's exchange-rate policy during a meeting of top Chinese economic and political leaders and their U.S. counterparts in Washington on May 9 and 10. Since China let its currency float somewhat in mid-June 2010, it has appreciated 5%.

"The [World Bank] projections certainly weaken the case for Chinese currency policy being a significant deterrent to the adjustment of global macroeconomic imbalances," said Brookings Institution economist Eswar Prasad, who says he isn't convinced that China has decided to rely less on trade surpluses to power its growth.

However, World Bank economists said that a rising yuan exchange rate could be a key policy tool for China to control inflation. "If you have inflationary pressures, appreciating the exchange rate can help you with that," Mr. Kuijs said. A rising yuan would reduce the cost of imported goods, particularly commodities and resources, thus relieving cost pressures on Chinese companies and consumers.

In 2011 and 2012, the World Bank forecast on Thursday, China's trade surplus would contribute an average of just 0.2 percentage point to its projected 9% economic growth; the World Bank's raised forecasts to 9.3% growth this year and 8.7% next year. That is a big decline from last year when the trade surplus accounted for 0.8 percentage point of China's 10.3% GDP growth. During the middle of the past decade, trade surplus often accounted for about 2.4 percentage points of China's annual growth.

GDP is a measure of all goods and services produced in an economy. In GDP accounting, exports add to the total and imports subtract from it. The overall trade surplus or deficit either adds or subtracts from GDP growth.

"Net trade"—exports minus imports—"should be broadly neutral with respect to growth" over the next two years, the World Bank report concluded.

International trade has transformed the Chinese economy. Three decades ago, it provided a way for an inward-looking Communist nation—whose per capita GDP in 1980 was $205, according to the International Monetary Fund—to put its vast numbers of workers to economically productive use.

Rather than rely on a tiny domestic market, the country's leaders welcomed foreign investors who built factories that exported to the world. Beijing essentially copied the export-led growth model of Japan and Korea, though it was far more open to foreign investment than its economic role models.

Trade's importance to the economy went well beyond the actual exports and imports. Much Chinese investment—the largest part of GDP growth over the past few decades—went to build the railways, ports, highways and airports necessary to make China a trade power. By last year, China had overtaken Germany as the world's largest exporter.

But Chinese exporters now say their job has gotten much tougher.

"We are facing so many problems for exporting, such as uncontrollable labor costs, rising cost of material, whose quality is out of control, and an unstable" value of the yuan, said Mao Peixin, owner of Shanghai Lituo Knitting Co., which makes sports socks and exports them mainly to the U.S. and Japan. There is also new competition from Vietnam and others trying to follow China on the path of export-led growth.

Mr. Mao said he is beginning to focus more on the domestic market, as China grows more wealthy, but he faces tough competition there as well. He says he plans to set up a plant to produce raw material in order to keep costs down. "We will offer more functional products to domestic consumers," he said.

China still has export growth that other countries would envy—12.4% in 2011, the World Bank forecasts, accounting for inflation. But that is only about half the rate that China routinely managed before the financial crisis in 2009.

In 2006, exports equaled 39.1% of China's GDP, a high-water mark. That plunged to 26.7% in

2009 as world trade crashed. Since then, exports' share of GDP has recovered somewhat, but the World Bank forecast that next year they will represent just 29.4% of the Chinese economy.

—Aaron Back and Kersten Zhang contributed to this article.

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