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Will China continue to be the engine of growth in the world☆

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1. Introduction

China was one of the fastest growing countries in the world since its transition from a planned economy to a market economy at the end of 1978. Before the transition, China was trapped in poverty for centuries. Its per capita income of US$154 in 1978, measured in current US dollar, was less than one-third of the average in Sub-Saharan African countries.[1] China was an inward-looking country as well, with trade dependence (trade-to-GDP) ratio merely 9.5 percent. China's growth since then has been phenomenal. Annual GDP growth averaged 9.7 percent over the 36-year period, and annual growth in international trade, measured in US dollar, at 16.4 percent. China becomes now an upper middle-income country, with a per capita GDP of US$7600 in 2014. More than 680 million people have escaped poverty. Its trade dependence ratio reached around 50 percent, the highest among the world's large economies. With such an extraordinary growth performance, China overtook Japan in 2009 as the world's second largest economy, replaced

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[1] Unless indicated otherwise, the statistics on the Chinese economy reported in the paper are from the *China Statistical Abstract 2015*, *China Compendium of Statistics 1949–2008*, various editions of the *China Statistical Yearbook*, published by China Statistics Press, and World Bank's World Development Indicators 2015 (http://data.worldbank.org/data-catalog/world-development-indicators?print).

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Germany as the world's largest exporter of merchandise in 2010, became the world's largest trading country in 2013 and, measured in purchasing power parity, overtook the U.S. in 2014 as the world's largest economy.

The spectacular growth over the past three decades not only has improved the wellbeing of Chinese people and China's global status but also has made China a stabilizing force and driver of growth in the world economy. In the sudden eruption of global financial crisis in 2008, China was the first country in the world to recover in 2009. Since then, China contributed each year more than 30 percent of global growth, helping the recoveries in other countries.

The coming crash of the Chinese economy, however, has reemerged as a popular view in the global media and international fora. The reason for such a doomsday prediction this time is the persistent deceleration of China's growth after 2010. The growth rate dropped from 10.6% in 2014 to 7.3% in 2014 and further down to 6.9% in 2015, which is the lowest record in 25 years. It is the first time for China to experience such an extended period of deceleration after the transition to a market economy in 1979. The downward pressure continues to be huge. This deceleration is commonly attributed to China's internal structural problems, such as inefficient state ownership, high debt leverage, ageing and an unsustainable investment-led growth model. Such structural problems are hard to solve. As such, a crash is believed unavoidable. The turmoil in the equity and foreign exchange markets since the second half of last year further reinforces this pessimism about China's future.

After eight years since the eruption of the global financial crisis in 2008, the high-income countries, including the U.S., has not fully recovered from the crisis and may be trapped in a secular stagnation (Summers, 2014). Whether China will be able to maintain dynamic growth is a paramount concern for the world economy. In this article, I will analyze why China was able to achieve such an extraordinary performance during its transition to market economy but not before its transition, why China crash was a repeated theme in the global media in spite of its extraordinary performance, and whether China will to continue be a growth engine in the world.

2. The reason for China's extraordinary performance after transition but not before

Rapid, sustained increase in per capita income is a modern phenomenon. Studies by economic historians, such as Angus Maddison (2001), show that average annual per capita income growth in the West was only 0.05 percent before the 18th century, jumping to about 1 percent in the 19th century and reaching about 2 percent in the 20th century. That means that per capita income in Europe took 1400 years to double before the 18th century, about 70 years in the 19th century, and 35 years thereafter.

A continuous stream of technological innovation is the basis for sustained growth in any economy. The dramatic surge in growth in modern times is a result of a paradigm shift in technological innovation. Before the industrial revolution in the 18th century, technological innovations were generated mostly by the experiences of craftsmen and farmers in their daily production. After the industrial revolution, experience-based innovation was increasingly replaced by field experimentation and, later, by science-based experiments conducted in scientific laboratories (Landes, 1998; Lin, 1995). This shift accelerated the rate of technological innovation, marking the coming of modern economic growth and contributing to the dramatic acceleration of income growth in the 19th and 20th centuries (Kuznets, 1966).

The industrial revolution not only accelerated the rate of technological innovation but also transformed industrial, economic, and social structures. Before the 18th century every economy was agrarian; 85 percent or more of the labor force worked in agriculture, mostly in self-sufficient