

# Over accumulation of Capital in Chinese Economy and OBOR: from a Japanese perspective

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# Contents

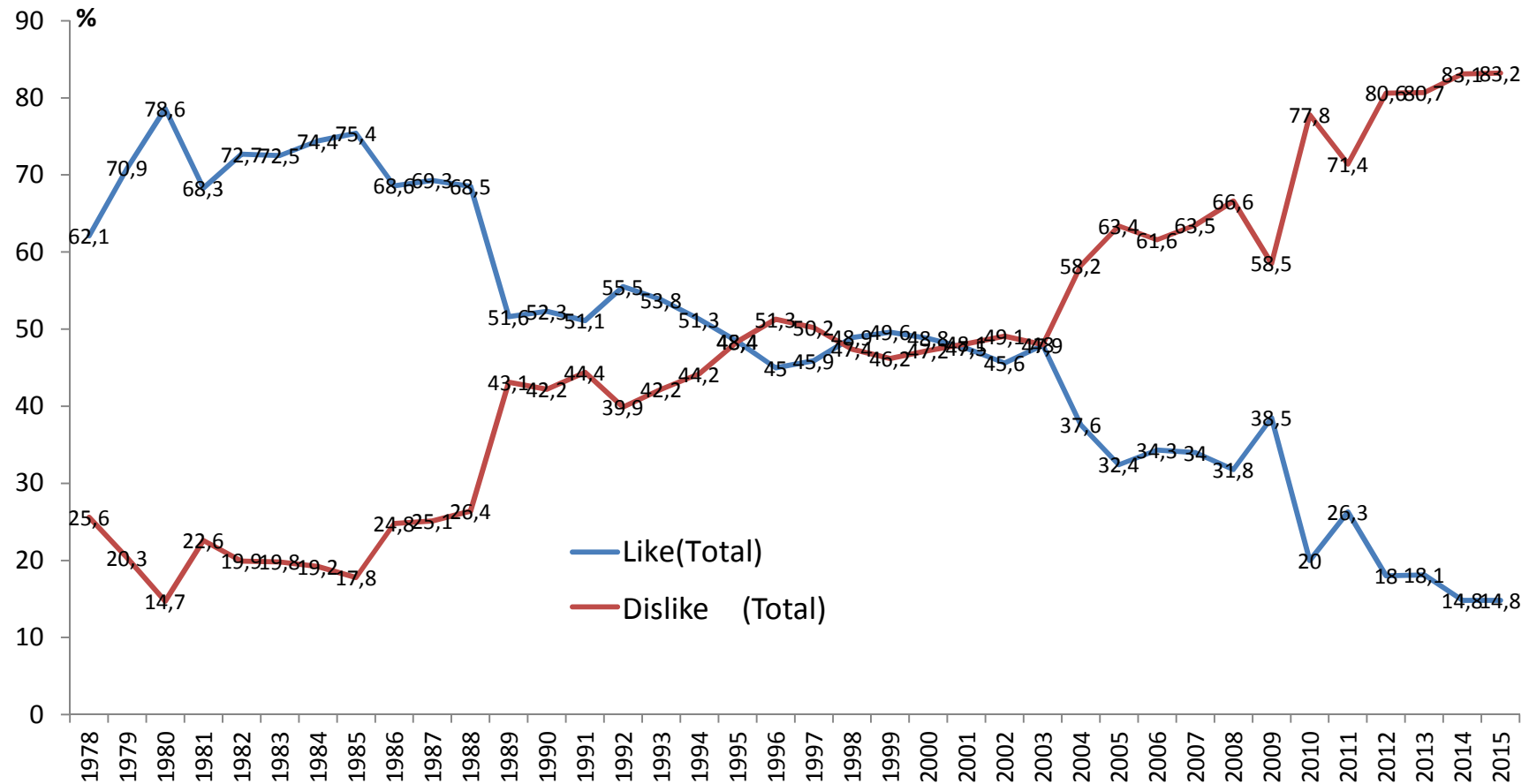
1. "uncertainty" about One belt, One road Initiative
2. The Estimation of Over Accumulation of Capital and Dynamic Inefficiency
3. Conclusion: Countermeasure of Japan

# 1. "Uncertainty" about One Belt, One Road Initiative

## ‘One Belt One Road (一帶一路)’ as “Too Political and Sensitive Matter” in Japan

- There is serious Dichotomy about the Recognition of China, in Japan, “Anti-China, else Pro-China (or Anti-US)”
- ⇒ This phenomenon throw a shadow on the analysis of Chinese Economy, because optimistic anticipation is often regarded as “taking pro-China position”!
- Background: Various survey data shows most of Japanese hold some unfavorable view of China, and the ratio is getting higher.

# Figure1. Sense of Intimacy against China



Source: Cabinet Office in Japan, <http://survey.gov-online.go.jp/h27/h27-gaiko/index.html>

# Question

- Why is there strong anti-China or pessimistic bias about in Japanese society, although there is win-win relationship about trade or direct investment?
- Except for more sensitive issues such as ongoing friction over maritime claims, some “uncertainty” of Chinese Economy seem to make Japanese people more pessimist about it, rather than reality.

# Chinese Economy and “Uncertainty”

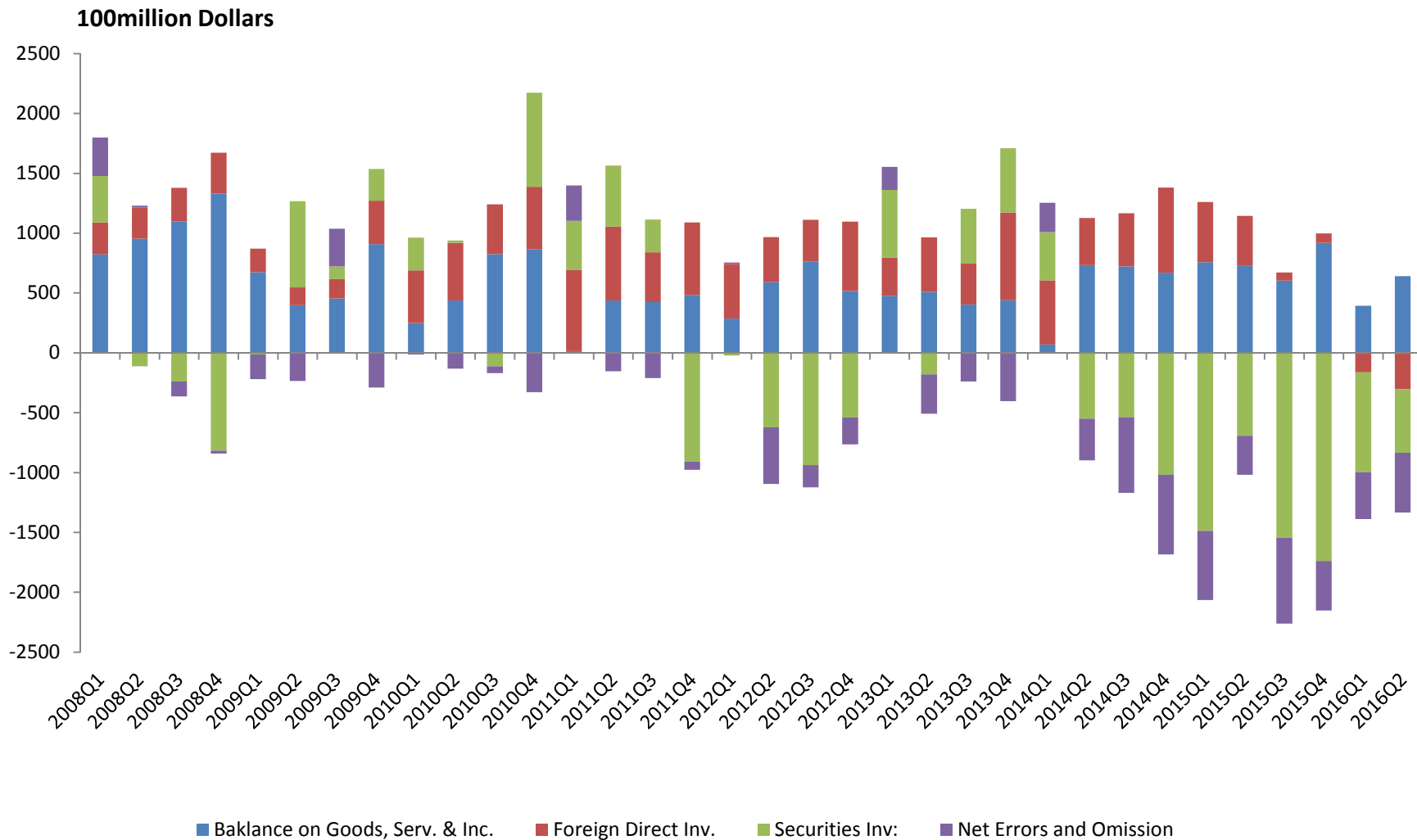
1. Statistics by which we measure the scale of the economic activity are uncertain, therefore, the risk the economy confront is difficult to calculate.
2. Economic “system” as the background of the economic phenomena are so different from those of the developed countries that it is difficult to image or understand it, offering the impression of “opacity” and “uncertain”.
3. Such a “not trenchancy system”, is not only the source of its own risk, **it has also become a factor of the dynamism** of Chinese economy.
4. There is the risk that the economic activity is often influenced by so many political issues or contradiction.

# The "Uncertainty" about One Belt, One Road Initiative (一帶一路)

1. the uncertainty of the productivity of the project
  2. the uncertainty about the domestic economy; the investment of infrastructure into the neighboring countries also has the effect to "let out" the domestic excess capital and to solve serious problem of excess supply capacity.
- ⇒ becoming "net exporter" of capital since 2014 (see Figure3)



# Figure3. Trend of Current Account



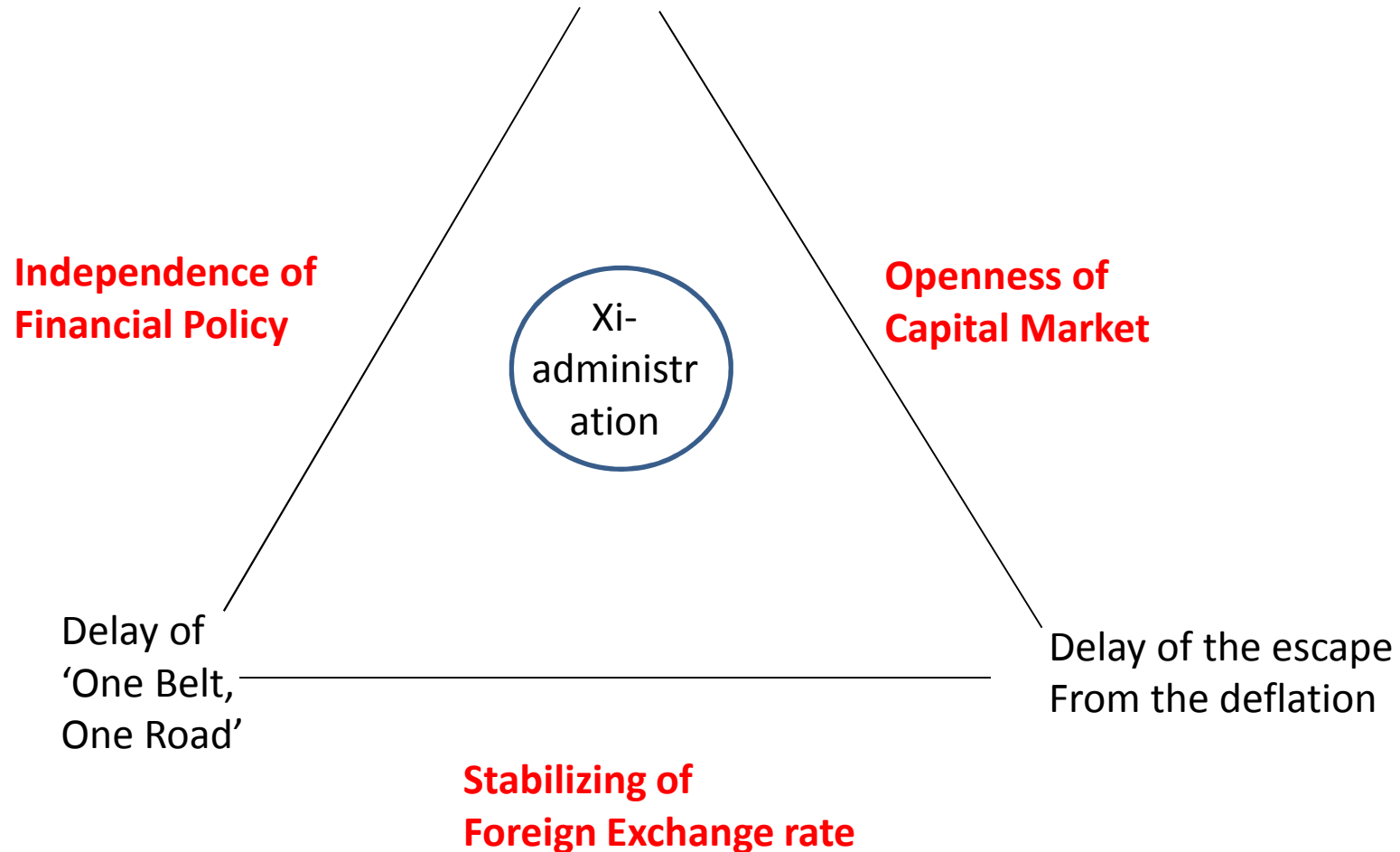
Source: State Administration of Foreign Exchange (<http://www.safe.gov.cn/>)

### 3. the uncertainty about the Internationalization of RMB

- Internationalization of RMB is necessary, if in the future **AIIB or Silk Road Fund** would like to implement the yuan-denominated lending against investment of infrastructure.
- However, ① aggressive foreign investment of infrastructure (One Belt and One Road), ② internationalization of the RMB, and ③ implementation of flexible financial policy,
- Out of these three goals only two could be realized at the same time at present, (**Impossible Trinity**).

# Figure4.Impossible trinity by Xi Jinping?

Delay of Internationalization of RMB



### 3. The Estimation of Over Accumulation of Capital

# What does “Over Accumulation of Capital” mean?

- As the capital stock is increasing, the return of fixed capital investment (marginal return of capital stock) is decreasing
  - Under some condition, while the capital stock is increasing, and **the return of fixed capital investment is getting smaller than the rate of economic development**, the fixed capital investment continues to expand.
- ⇒ “Over Accumulation of Capital” or “Dynamic Inefficiency”
- In this situation, the capital gain by the increasing of asset price fills the gap between return of investment and the time preference
- ⇒ **occurrence of the asset bubble**

# The Test of Dynamic Inefficiency

✂ two kinds of definition of dynamic inefficiency

(1) real growth rate of GDP  $>$  real capital interest rate

(2) the share of gross capital income  $>$  gross rate of fixed asset investment

✂ under the economy in which the financial market and level of interest is restrained, the criteria of (1) is not appreciate.

⇒ We tested whether China and other countries is under dynamically inefficient, using (2), Abel=Mankiw=Summers=Zeckhauser (1989)'s criteria.

## The several Issues about Statistics

### a. The data source on the factor incomes of GDP

- ① **the data of Financial Circulation** in national level, which is described in Chinese statistics yearbook  
⇒ **The labor compensation is overestimated**, because this estimation is based on the assumption that the growth rate of household income equal to the growth rate of labor compensation.
- ② **the data for each province** which is described in Department of National Accounts, National Bureau of Statistics of China(2007) and Chinese Statistical Yearbook/  
⇒ about the **investment rate**, the aggregate value of all provinces **is over-estimated** compared to the value of the national level.

# The Solution;

- About **the factor incomes of GDP**, we use the **aggregate value of provinces data**.
- **About the investment**, we use both the value of the national level and estimates using the data for each province.



## b. The Deduction of Self-Employed Person's Labor Income

- In 2004, China's macroeconomic statistics system has been changed from the old SNA system to 93SNA system.
- The labor compensation of the self-employed person is not include in 93SNA's "compensation of employees," so the labor share is underestimated in 93SNA system.

# How should we estimate it?

- **First.** Estimate the ratio of mixed income and the operating surplus
- **Second.** Estimate the labor income of manager, multiply the 0.33 to the mixed income.
- **Third:** Deduct the estimated the labor income of manager and workers, and taxes (minus subsidies) from the GDP .

## C. On the **stock increase**

- In the GDP data of China, increase of inventory, is up to about 5-8% of GDP until the late 1990s, relative large share.
- It can be because that the definitions of " increase of inventory " or the economic structure of China is different from the United States and Japan.
- We will show **both of the estimation results, total capital formation and the total fixed capital formation**, as the data of the investment.

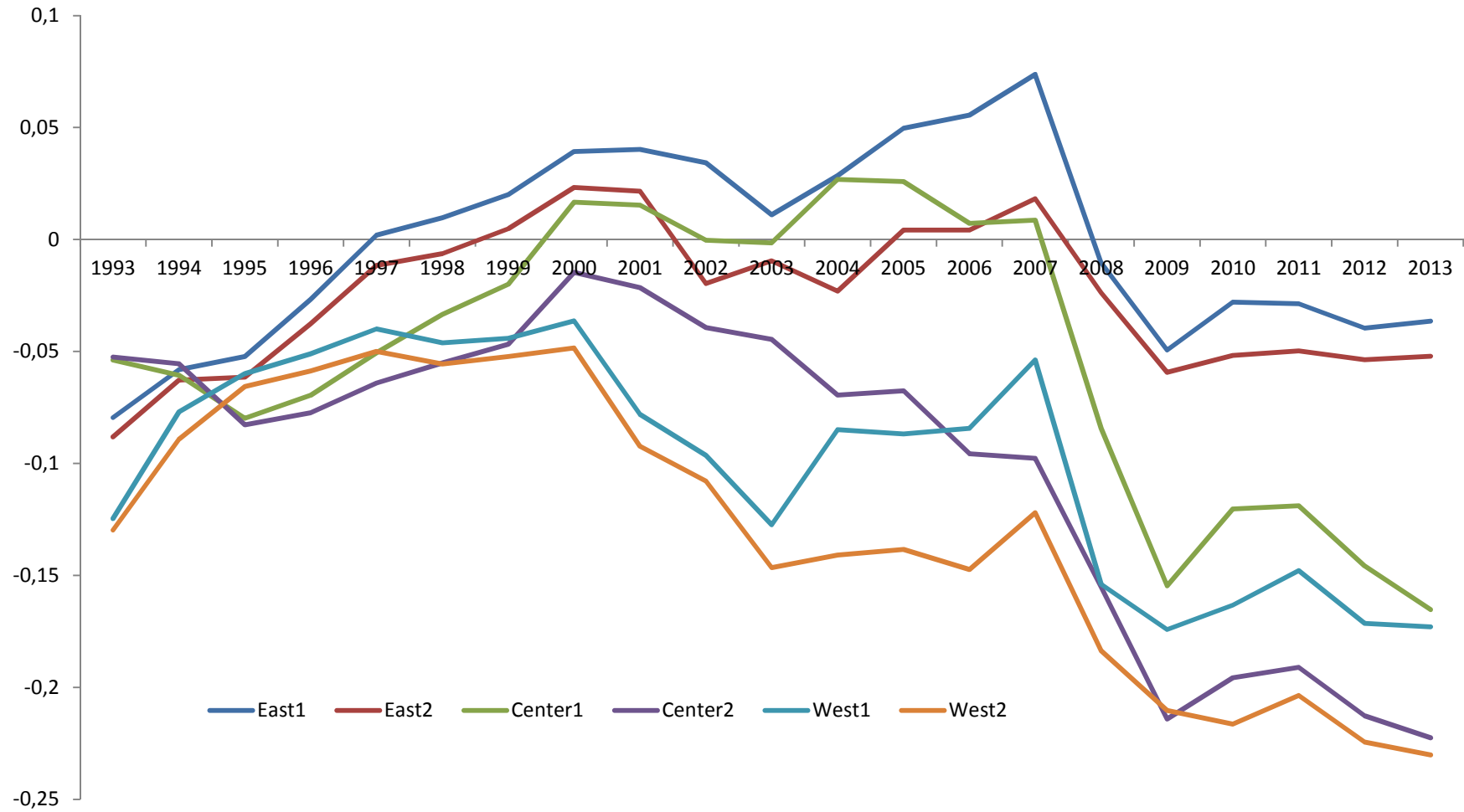
# The Method of Estimation about AMSZ Criteria

	Deduction of Enterprises Owner's Income	Data of the Investment	Method of Estimation about Investment
A	No	Gross Capital Formation	Aggregated Data of Provinces
B	Yes	Gross Capital Formation	Aggregated Data of Provinces
C	No	Gross Capital Formation	National Data
D	Yes	Gross Capital Formation	National Data
E	No	Gross Fixed Capital Formation	National Data
F	Yes	Gross Fixes Capital Formation	National Data

# Figure5 The Estimate of Dynamically Inefficiency, China



# Figure 6. Dynamically Inefficiency in Each Region, China



# The Empirical Result

- 1993—2000: in most of estimation AMSZ criteria are minus, but **the condition about OAC has been improved**
  - 2001—2007: In the estimation in which the labor compensation of the self-employed person is deducted (B, D, F) AMSZ criteria are minus. And the figures show that OAM were getting more severe year by year.
  - 2008—2014: **Every estimation show AMSZ criteria is minus**, meaning that OAC in Chinese Economy has been very severe after Lehman Shock.
  - About estimation of each region, Center and Western Area's OAC has been more serious than Eastern Area.
- ⇒ Because of **increasing of fixed investment in inland area**, whose productivity is very low, as public financial policy.

### **3. Conclusion: Countermeasure of Japan**



# The Background of “Over Accumulation of Capital ”

- ① Aggressive investment by the local governments and local enterprises, especially after Lehman Shock, 2008.
  - ② Decreasing of distribution to the labor
  - ③ Increase in retained profit of the enterprises
  - ④ High saving propensity of households
- ✘ These situation is clearly not sustainable, and OBOR is needed for “soft landing” of OAC.

# How Japan confront OBOR and uncertainty of Chinese Economy?

1. We should understand the reality of Chinese Economy, and discuss the future of OBOR or AIIB, to avoid too pessimistic or anti-China biased view.
2. We should positively propose Chinese government or well-informed person the prescription for problem of domestic economy, based on the experience of Japanese “lost 20 years”.
3. We also should positively propose the way of reform about current International financial regime represented by IMF, to avoid making China rush into the Internationalization of RMB.

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