

# Influences for China with Reformation of the Supply Side

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**Abstract:** With decades of high-speed development, China has become one of middle income countries (MICs). But with plenty of risk accumulation as deduction of demographic dividend, trap of MICs, adjustment of global economic structure and approaches, Chinese economic development has entered into New Normal. Chinese economy faces big change. For getting used to it, it's urge to perfected environment of supply-side while optimizing environment of demand-side. For understanding how the reformation effect on Chinese economy, this paper provides detailed suggestions, with examples, for writing the background, method, results, and conclusion sections. The primary goal of the paper is figure out that definition of the reform, why need it, and how it will be. Combine data and research results trusted to make conclusion.

**Keywords:** Economic Structure, New Normal, Change, Supply-side.

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## 1. INTRODUCTION

### 1.1. Background:

With over thirty-year of reform and opening up, Chinese economy has been keeping high growth, and had succeed to be a middle-income country. China has become the world's economic power. However, with adjustment of the international economic structure, the middle-income trap risk, the demographic dividend, and a series of internal and external factors, Chinese economic development entered a new period, New Normal.

Since 2008, global economy has entered recession situation. With the background of world-wide, Chinese economy has slowed down, from 9.6% in 2008 to 6.9% in 2015. What are the reasons? One is overcapacity, irrational economy structure, investment demand is curbed. The other one is that repayment pressure restricts investment. According to that, the demand side cause economy imbalance with the background of New Normal. Somehow, the root cause is, structural imbalance, it means that effective supply cannot match the change of market demand, serious structural overcapacity. There, short-term stimulation of demand side became weaker. On the contrary, supply side management became more important and targeted to decrease structural imbalance.

This paper reports the findings of a thorough study to establish the factors that have caused Supply Side Reform, how it work, what is the influence.

To learn the contents of Supply Side Reformation approaches, it needs to understand global economic environment, Chinese economy situation, policy, procedures, and the demographic issue, the situation of supply and demand, etc.

### 1.2. Research Significance:

The purpose of this paper is to understand what Reformation of Supply Side exactly is, and how it affects Chinese economy. Meanwhile, there are some contributions attached.

### 1.3. The Scope of the Study:

The scope of the study includes Chinese current economic situation, the contents of Supply Side Reformation, the situation and influence of existing policies operation.

In this study therefore, wish to fully understand Chinese economy dilemmas and outlet, and try to identify the factors that influence Supply Side Reformation, economic, political, sociological environments of operation among Chinese society.

#### 1.4. Objectives of the Study:

- Definition of the Reformation of Supply Side
- Understand current economic situation in China
- Identify the factors that influence Supply Side Reformation
- Analysis existing policies
- Suggest practical ways for further reformation

## 2. LITERATURE REVIEW

### 2.1. Definition of Supply Side Reformation:

The subject of Supply Side Reformation is economic structural adjustment, achieving economic factors to be the most optimized to improve the quality and quantity of economic development. Economic development transfer from demand side to supply side. The factors of demand side are investment, consumption, export. The factors of supply side are labor force, land, capital and innovation.

The core of the Supply Side Reform is that market plays a decisive role in the resource allocation, enterprises, entrepreneurs and approaches play leading role in economic development. Meanwhile, reducing executive interference, stimulating market vitality, transforming functions of government. Moreover, fostering new developing drives through comprehensive reformation, creating new points of economic growth through comprehensive innovation, achieving sustainable development of economy through full productions elements. Developing new industries, respecting and obeying economic law and market law, removing overcapacity, avoiding waste of resource. Also, encouraging development of new industry, new technology and approaches rapidly.

President Xi Jinping put forward the idea of Supply Side Reform on Nov 11<sup>st</sup>, 2015, which has led the guiding principle for policy making. In the process of economics development, there were two macroeconomics propositions: short-term demand management and short-term supply management. However, in the long-run, the key to drive economic growth is from supply-side, involved science and technology, human capital, material capital, industrial structure, economic system, and so on. The main of the reformation is that improve product's quality.

### 2.2. The Relationship of Supply Side Structural Reformation and Supply-side Economics:

Both of Supply Side Structural Reformation and Supply-side Economics focus on aspects of supply side in economy. However, the core of Chinese Supply Side Structural Reformation is economic structural adjustment and economic development change, improve total factor productivity through improving adaptation and flexibility of supply and demand's structure. The reformation is based on the political economy of socialism with Chinese characteristics, the purpose of the reformation is to develop and improve the socialist market economy, consolidate the basic socialist economic system and improve the living standards of the people. As for American supply-side economics is represent that the thought of neoliberalism, and the sets of policies is for increasing the income standards of the rich, repair capitalism system. The appearance of it is that decrease taxation, especially for the rich, release governance to solve the problem of stagflation. Misunderstanding the Reformation of Supply Side could cause problem to China's economic development. Therefore, while putting forward to the reformation, people should make it clear that the gap between them.

### 2.3. Research Outcomes:

From Supply-side Economics, the beginning of Supply-side study to Chinese Supply-side Structure Reformation now, the study is involved lots of areas and divided into many schools. As for this paper, it is going to make a summary according study fields approximately.

#### ➤ Theoretical Logic of Supply Side Reformation:

Su Jian & Lin Weibin (2016) proposed that Supply Side Reformation means Chinese macroeconomic management policy adjustment take place in two aspects. Firstly, it would focus on supply-side management. Secondly, the way of previous management should be changed. In the situation of the unbalance between demand and supply, consider that, it is

necessary to promote the reformation. For realizing this goal, it requires that break through systemic obstacle, make market can play decisive role in resource allowance, optimize combination of productive elements. On the other hand, it requires that government should execute the duty on aspects of policy guidance, supervisory and constraint, public service, and.

➤ Yang Dongwei (2016) suggested that demand side and supply side are not absolutely opposite theories, and Chinese economic policy never ever absolutely rely on either of them. What's more, Supply-side Reformation requires that economic policy and policy of social development should be more harmonious. The reason of that is, except for productive elements, most of supply-side elements are belong to social category, as labor force factor, citizen's environmental awareness, etc. Therefore, the macroeconomic transitional mission would expand to the whole department from economic department. Like, the aspect of labor supply optimized, Population and Family Department is supposed to study that how to manage the issue about aging before getting rich with the background of Lewis Turning-Point. As for Labor and Social Security Department need to study solution of postponed retirement to ensure per capita labor force to support the population is in rational section. And these departments will be supposed to consider economic issue by supply-side thought.

➤ **Practical Path of Supply Side Reformation:**

Teng Tai (2016) mentioned that too many Chinese industries is at aging stage. The new study believed that supply doesn't create capability of self-demand. And new supply and new demand are from wealth of knowledge, wealth of information, wealth of culture, wealth of finance and other social services approaches. In other word, they came from human thinking and activity. Those intelligence contribution reach 79% in American economic field approximately, but only contribute 49% in China. Hereby, how to stimulate people's creation, then apply it into production, that is the problem should be solved.

Li Jin (2016) put forward that the way to solve the issue of decentralization is that reform state-owned enterprises. Firstly, transfer theoretical drive to practical drive; secondly, transfer upper-class power to middle-class power; thirdly, government force transfers into enterprise force. For this consideration, he believed that supply is a tool to consumption. Like, if not large-scale engineering activities, cement and steel's industries could be down. And he also thought about reorganization for improving higher standards of consumption and supply, to manage "zombie enterprises"<sup>1</sup> to encourage the market-oriented allocation of resources.

Mao Yanbing & Sun Kai (May, 2016) proposed that current economic issue in China is structural problem but periodic case. The final goal for the reform is that accomplish product quality improvement. For this concern, writers suggested that start from the end of product, adjust industrial structure, optimize product element allocation, encourage market system to operate adjustment function, increase total factor productivity, maintain financial market stable, take full advantage of system safeguard. They encouraged that prepare various ways to put into the Supply Side Structural Reformation.

➤ **The Core of the Supply Side Reformation:**

*Fan Di* (2016) proposed that the three challenges to Supply-side Economic Reform in China, low consumption, capital mismanagement and rising costs. He believes that extreme income inequality leads to false picture of prosperity and distorted supply and demand. And the reason lead insufficient domestic demand and strong dependence on overseas markets: large income disparity. It seems like people who live have living standard of developing countries but live in developed countries. The huge income inequality is the cause of low internal consumption and serious distortion in China's economic structure. In recent years, China's financial sector experienced an oversupply of money and extraordinary credit growth. Meanwhile, economic growth kept declining and credit funding was not able to flow into the real economy, lots of money deposited in financial transactions never enters the business entities. Where does it go? One way is to keep debt cycle and Ponzi financing by paying off old loans with new loads. The other way is for stock market bubble. The oversupplies like a black holes swallow up funding. And the capital will turn into hard asset that will continue to consume resource, rely on more debt turnover. Eventually becoming part of the Ponzi finance pattern.

Combine the saying above and articles involved, the main challenge of Chinese economy is structural issue, overcapacity,

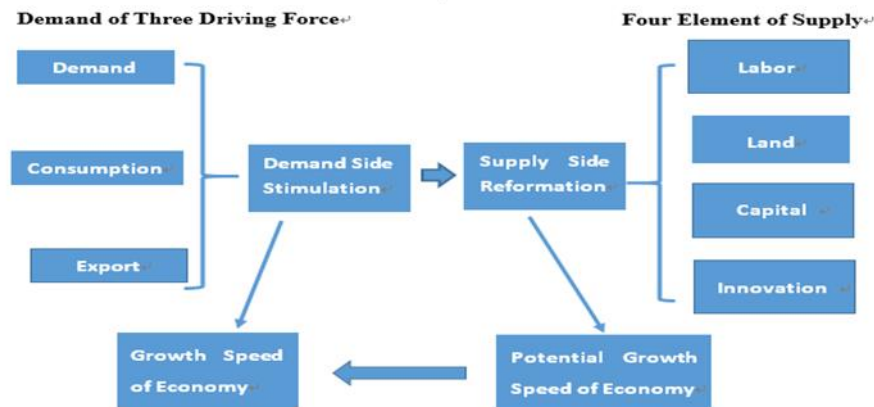
<sup>1</sup> Zombie enterprise is an economic concept, it refers to debt-laden enterprises that cannot be revived but cannot be closed for some reason also.

insufficient valid demand, the cost of manufacture is over high. And researcher pay attention to figure the cause of Supply Side Reformation out as the figure 1 and figure 2 are followed.



Source: National Bureau of Statistics of China

Figure 1: Process of Supply Side Reformation



Source: Wallstreetcn.com

Figure 2: the Relationship of Demand Side of Three Driving Force and Four Elements of Supply Side

The potential factor of medium-and-long-term economic growth is the growth of the four elements. Therefore, the purpose of structural reformation is to adjust economic structure to achieve the growth of economic amount and quality.

### 3. METHODOLOGY

This study is using the qualitative methods in comprising the facts found in literatures related to the topic. In addition to data collection from the websites, the National Bureau of Statistics of China and approaches. Some points of views and different kinds of perspective from scholars, researchers and analysts, who have been working on the field and seen the development.

#### 3.1. Data Collection Method:

The study aimed to figure out what the influences of Supply Side Reformation in China. As for this consideration, should make it clear that the variables to influences of the reformation. The thesis utilize quantitative analysis to analyze influence which will be brought by the reformation of the supply side. The reason of utilization quantitative analysis is to combine data passed and Chinese current situation to acquire related objective conclusions.

Analysis will involve data of economic region, financial region, policies region and system region which include GDP, GDP growth, economic structures, industrial structures, CPI, international finance etc. All data are from National Bureau of Statistics of China and the People's Bank of China and approaches.

The thesis analyzes the reason why Chinese government decided to implement the Reformation of Supply Side step by step. Combine GDP, GDP growth, industrial growth, economic structures and CPI etc. during past five years to explain what the problems of China economy are and why the speed of Chinese economic growth is slower than before. Combine data found to analyze the reasons of reformation from surface to interior. In final, it will acquire conclusions by comprehensive analysis and advice workable recommendations.

#### 3.2. Data Analysis Method:

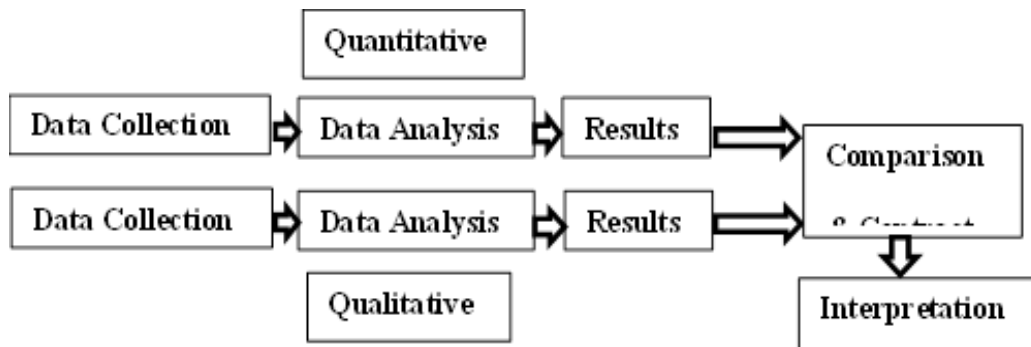
By looking though literatures, the data and outcomes will be gathered by in-depth analyze, part of them would be out from privilege research results and other policy-activities, take them as references. Somehow, as a result the analysis will

be qualitative, and there will be a few of quantitative solutions.

### 3.3. Comparative Analysis

By comparing the Chinese economic situation before and after the reform, this study tries to figure out that how the reformation effect on Chinese society, where was it, why put it forward; where will it go and how will it be.

3.4. **Qualitative and Quantitative Analysis:** Research process for mixed method.



## 4. FACTS AND FINDINGS

This chapter will discuss the results that have found in relation to both research questions and existing knowledge. In order to put forward accurate findings and recommendation about the influences, tools that are used analyze the situation of China and compare current with past situation. As mentioned in earlier chapter, the raw data used is from authorized websites and organizations. Furthermore, the data operated is following scientific calculation.

### 4.1. The Chinese social situation:

This part will cover the current situation of Chinese society. Also, these data analysis are variables to effect on Supply Side Reformation.

#### 4.1.1. Situation of GDP Growth:



Source: National Bureau of Statistics of China

Figure 3: The Annual Growth Rate of GDP from 2011 to 2015

According to figures above, what they show is that Chinese economy still cannot get out of the trouble of the American subprime mortgage crisis and European debt crisis. Before the Reformation of Supply Side, Chinese economy relied on factors of demand side, investment, export and consumption. However, the great recession led these factors to go down, and it limited development of Chinese economy sharply. Both of international market and domestic market lost investment confidence, lack of foreign capital, market value evaporation, etc. Inadequate demand of global market is the first challenge.

With the Supply-side Structural Reformation going further, the effect has come out little by little. According to data published by National Bureau of Statistics of China on July 15<sup>th</sup>, year-on-year Chinese GDP growth rate is 6.7% in first half year. And both of the first quarter and the second quarter are 6.7%. The growth rate reached the goal about growth rate 6.5% - 7% which put forward in the government work report at the beginning of this year. Even though, GDP growth rate is not as high as before for the reformation's reason, the trend is still positive. Here are some data from IMF about economic growth comparison. Chinese economic growth went down from 6.9% to 6.6%, but still higher than developing countries GDP. The growth rate is not that good as before the Supply-side Reformation, but it is more healthy, green and positive.

#### 4.1.2. Situation of Foreign Trade in China:

The annual growth rate of export value shows that Chinese export has faced big pressures and challenges. Chinese economy has been always relying on foreign trade, and the U.S.A is the one of the source of trade surplus. Therefore, the turndown of American economy and the global credit crunch led the external environment of China into high pressure. Because of economic contraction in international market, general trade got impact seriously, plus high base last year, so the value of export decreased sharply.

For hysteric nature, it cannot show negative effect up at once. Fortunately, with internal adjustment inside industries, stimulating policies and the situation of external demand, the order got recovery in the next half year.

Chinese trade was in the toughest situation in 2009 since 21<sup>st</sup> century. To handle sharply impact of global economic crisis, Chinese government put forward sets of policies and measures, completed export tax rebate policy, advanced trade financing environment, expand coverage of export credit insurance for maintaining external demand stable. Also, Chinese government worked hard on expand internal demand, like encourage import activities. With global economy and international market getting better, the condition of import and export has improved. According to the data released by WTO, China's export in 2009 accounted for the proportion of global exports from 8.9% to 9.6%, it has overtaken Germany as the biggest nation of export.

**Table 1: World Output**

	2014	2015	2016	2017
<i>Advanced</i>	3.4%	3.2%	3.1%	3.4%
<i>United States</i>	1.9%	2.1%	1.6%	1.8%
<i>Euro Area</i>	2.4%	2.6%	1.6%	1.8%
<i>Other Advanced</i>	2.8%	2.0%	2.0%	2.3%
<i>China</i>	7.3%	6.9%	6.6%	6.2%
<i>ASEAN 5<sup>2</sup></i>	4.6%	4.8%	4.8%	5.1%

Source: International Monetary Fund, Oct, 2016

According to government work report in the beginning of the year, target of economic growth was set 6.5% to 7%. It is easy to know that economic growth is 6.6% from table. This result accord with target which was set by work report. Although growth is slower than before, it still keeps middle and high growth. And it is also expectation of reformation of the supply side. Therefore, it could say reformation of the supply side is positive for Chinese economy and it is helpful to make Chinese economy keep middle-high growth in the future.

#### 4.1.3. Industrial Problem Analysis:

**Table 2: the Annual Growth Rate of Added-value of Three Industries**

	2012	2013	2014	2015
<b>the Primary Industry</b>	9.31%	8.70%	5.44%	4.33%
<b>the Second Industry</b>	7.53%	6.92%	9.59%	0.93%
<b>the Tertiary Industry</b>	13.26%	13.52%	10.85%	11.69%

Source: National Bureau of Statistics of China

The tertiary industry is going to be stronger and take the dominated position in the whole industry. And the second industry has been entering into challenge since 2014. There are three key points lead to this result.

Economic growth downward. In the first quarter to the third quarter of 2015, the year-on-year growth of GDP are 7%, 7% and 6.9%, average lower than last year 0.3%. Economic growth downward, domestic demand decreased, the growth rate of the fixed capital investment is at the lowest point in the late 15years. In addition, the global economic recovery slowly, the growth rate of Chinese export decrease 2%, the economic growth rate of the whole year 2015 pulled trend of price down.

<sup>2</sup> ASEAN 5's member countries: Indonesia, Malaysia, Philippines, Singapore, and Thailand.

The price of international commodity tumbled. Till October, 2015, IMF published IPCP has dropped to 102.99, the lowest point since 2009. Oil price has dropped 55.27%, food, technological raw material and agricultural products prices have dropped 27.55%, 27.27% and 22.16%, in accordingly. The price indicators of Fuel and ferrous metal decline in the most. Therefore, international commodity price decline effect on trends of Chinese PPI and PPIRM, and the main reason to decline of Chinese PPI and PPIRM is international energy price drop sharply.

#### **4.2. Economy Improved and Developed in Stable Situation:**

In May, scale industrial addition value increased 6% year-on-year, and it was same as April. For Service industry, service production index was same as April. For employment situation, According to the data who was offered by Department of People and Social Security, Cities and towns employment increased 5 million and 770 thousand from January to May, it completed 57.7% of annual goal.

Price was steady. CPI increased 2% year-on-year in May, and it decreased 0.3%, compared with April. Decreasing amplitude of PPI reduced to -2.8%, it showed that change of supply and demand relationship of industrial products was positive.

Chinese economy promoted mainly be showed in aspect of structural adjustment and transition upgrade.

For industrial structure, service industrial growth was faster than industry. It means percentage of service industry in GDP was increase. For industrial internal structure, high-tech industry and forward equipment production industry kept high growth. It means that industry is forward to middle and high level.

For investment structure, investment structure continue to be improved. High-tech and service industry investment kept high growth.

For consumption upgrade, it kept related high growth that sale is relevant with improvement and perfected quality of citizens consumption.

These structures changed is the objective of reformation of the supply side. It aims to change structures and improve products' quality. Structure adjustment and changed would make China economy development more reasonable and steady. A reasonable and stable economy just achieves sustainable development in the future.

Structural adjustment makes Chinese economy have more ways to face more and more challenges and unsure factors. Structural adjustment can activate three driving force and make China economy keep high growth all the time.

## **5. CONCLUSIONS AND RECOMMENDATIONS**

This thesis introduced how Supply Side Reformation effect on China from several aspects, with analysis of Chinese current situation and comparison of current and past situation. This part will make conclusions and recommendation which are based on literature used and personal knowledge.

### **5.1. Conclusions:**

With over 30-year-development, Chinese economy entered into a New Normal under background of global recession. Old models of development would not be suit for further development. Time to get adjustment. For achieving economic power, this goal, China should seek new key of economic growth.

#### **5.1.1. The Necessity of Structure Adjustment:**

Select the superior and eliminate the inferior. As the country's economic development has entered a New Normal – with the growth rate having eased a notch, the overall structural reforms have been struggle and the previous stimulus package has yet to fully pay off. This is a difficult period known as the “triple-hazard stage”, unreasonable economy structure is the obstacle to further development, which means should get rid of industries with high consumption and low efficiency. Supply Side Reformation serves for it.

Making macro-policy steady, offering a stable macroeconomic environment. Maintain to implement positive financial policy and stable monetary policy, combine both and cooperate them. Under the background of global economy recession, the problem of international market have worse impacts on domestic market, and the deep conflicts are getting worse, the real economy is being trouble.

Accurate positioning the direction of the reformation. In recent years, the overall of economic structure has been optimizing, tertiary industry is playing a more important role in economic development. However, the structural conflict is still. The potential of the tertiary industry is still large. Compared with 70% of tertiary industry in developed countries as Europe and United States, China's tertiary industry is less than 50% of the total economic output. Furthermore, traditional industries is the majority in China's industrial system, it's hard for new industries to cover the recession of traditional industries. The obstacle of internal structure is purely clear.

As for the external economy, which has been great challenging to say the least in recent years. The dimension is that how to deal with reasonably fast growth under the background of global recession caused by the US sub-prime crisis of 2008 and the following credit crunch everywhere. And the slow recovery of the US economy has been preventing the global economy from speedier recovery, while impacting China's growth rate with shrinking imports. That, naturally, is another reason why the Supply Side Reform should be stepped up.

### **5.1.2. Core Contents of Supply Side Reformation:**

As mentioned in earlier chapter, the core content of Supply Side Reformation should be three keys, and it followed below.

#### **5.1.2.1. Product Quality Improvement:**

Quality is the key to product, no matter what kinds of product be offered, tangible or intangible, manufacturing products, commercial products, entertainment products and other else. Quality products is useful to maintain customer satisfaction and loyalty, and reduce the risk and cost of replacing inferior goods. Companies can count on it to build a reputation for quality by gaining accreditation with a recognized quality standard. The knowledge mentioned above is the basic economic common. Chinese government has been working hard on Supply Side Reformation, because product quality improvement issue doesn't only belong to enterprises, but also rely on government adjustment and macro-control. *Made in China* is not China's goal, *Created in China* is. According to report on the work of the government, China plans to enhance the quality and standards for consumer goods through more market-oriented measures and adopting wider range of global standards in the next five years. The step is part of national Supply Side Structural Reform and boosting domestic consumption.

#### **5.1.2.2 Innovation Encouragement:**

Innovation is the essence of sustainable development. The way to encourage innovation, the way to show the wisdom of government. China's State Council announced a string of new policies to encourage innovation as the country seeks to foster new engines for growth. *National Innovation Demonstration Zone* would be set up, including Beijing's Zhongguancun and Shanghai's Zhangjiang high tech zone, have been created to pilot new ideas and development models for use nationwide. Expansion of the program is aimed at fostering trailblazers for Chinese economic restructuring and transformation, according to statement, which one chaired by Premier Li Keqiang.

Government intervention will be further reduced to create an amicable environment for business start-ups and innovation. To boost employment and sustain growth, the Chinese government has stressed the role of innovation and entrepreneurship in its 13<sup>th</sup> five-year plan. A wide range of measures has been unveiled, including financial support, facility construction and administrative assistance, for start-ups. Also, Belt and Road and AIIB are innovation based on ancient Silk Road and World Bank. Ways of innovation are diversity, but it still working on further development.

#### **5.1.2.3 Service for Five Major Development Concepts**

New thoughts needs new concept to support. The main content of Five Major Development Concepts includes Innovation, Coordination, Green, Openness and Sharing. It could know that the objective of reformation is to promote economy further development and improve living standard and quality. Sharing refers to share economic achievement with others. Making people get benefit from social development. The more benefit they gain, the more positive to join production development. As for Green, with society developing, should get rid of something out of style, like development with sacrificing environment, and high energy-consumption industry, etc.

### **5.2. Recommendations:**

Based on literatures reading and personal knowledge, two recommendations as followed.



**5.2.1. Maintaining Steady Reformation Development:**

Rome wasn't built in a day, reformation also needs to be proceed step by step. For avoiding huge impact, it needs more patient while reformation is proceeding. After all, stable social environment offers chance to social reformation and development. Economic development should follow economic construction planning, proceed it step by step, making adjustments properly. During the process, lots of unpredictable risk and conflicts can impact on development. They do make sense to cost control and the result of the reformation. There are many reasons to believe that Chinese central government has ability to manage state and society. Also, China will welcome to world with more open and confident attitude.

**5.2.2. Don't Make a Buzzword but Little Progress:**

Since 2018, the central government put forward that plan to manage overcapacity issue in the steel sector. With the popular of the plan, lots of local governments resorted to drastic measures like bombing steel plants, to conform to the set quotas, rather than tackling the issue at the grassroots level. On the contrary, most official now urge companies to switch off facilities temporarily. Most of these unites restart production when the prices improve, adding to the already excess inventories. Hereby, the central government has failed to issue a coordination plan, to help local governments tackle potential problems that may arise during the capacity elimination process.

Industry experts said that the lack of clarity in targets and the methods for reform have hampered the smooth progress of Supply-side Reformation. At stake are issues like whether the central government or the market should play a bigger role and the intertwining of restructuring proposals floated by central and local governments. The central government should deal with the whole blue-picture, and local government implement it with self-owned personalities.

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