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China and the American Jobs Machine

China's export policy is really a social policy, designed to maintain order.

By [ROBERT B. REICH](#)

President Barack Obama says he wants to "rebalance" the economic relationship between China and the U.S. as part of his plan to restart the American jobs machine. "We cannot go back," he said in September, "to an era where the Chinese . . . just are selling everything to us, we're taking out a bunch of credit-card debt or home equity loans, but we're not selling anything to them." He hopes that hundreds of millions of Chinese consumers will make up for the inability of American consumers to return to debt-binge spending.

This is wishful thinking. True, the Chinese market is huge and growing fast. By 2009, China was second only to the U.S. in computer sales, with a larger proportion of first-time buyers. It already had more cell-phone users. And excluding SUVs, last year Chinese consumers bought as many cars as Americans (as recently as 2006, Americans bought twice as many).

Even as the U.S. government was bailing out General Motors and Chrysler, the two firms' sales in China were soaring; GM's sales there are almost 50% higher this year than last. Proctor & Gamble is so well-established in China that many Chinese think its products (such as green-tea-flavored Crest toothpaste) are Chinese brands. If the Chinese economy continues to grow at or near its current rate and the benefits of that growth trickle down to 1.3 billion Chinese consumers, the country would become the largest shopping bazaar in the history of the world. They'll be driving over a billion cars and will be the world's biggest purchasers of household electronics, clothing, appliances and almost everything else produced on the planet.

But in fact China is heading in the opposite direction of "rebalancing." Its productive capacity keeps soaring, but Chinese consumers are taking home a shrinking proportion of the total economy. Last year, personal consumption in China amounted to only 35% of the Chinese economy; 10 years ago consumption was almost 50%. Capital investment, by contrast, rose to 44% from 35% over the decade.

China's capital spending is on the way to exceeding that of the U.S., but its consumer spending is barely a sixth as large. Chinese companies are plowing their rising profits back into more productive capacity—additional factories, more equipment, new technologies. China's massive \$600 billion stimulus package has been directed at further enlarging China's productive capacity rather than consumption. So where will this productive capacity go if not to Chinese consumers? Net exports to other nations, especially the U.S. and Europe.

Many explanations have been offered for the parsimony of Chinese consumers. Social safety-nets are still inadequate, so Chinese families have to cover the costs of health care,

education and retirement. Young Chinese men outnumber young Chinese women by a wide margin, so households with sons have to accumulate and save enough assets to compete in the marriage market. Chinese society is aging quickly because the government has kept a tight lid on population growth for three decades, with the result that households are supporting lots of elderly dependents.

But the larger explanation for Chinese frugality is that the nation is oriented to production, not consumption. China wants to become the world's pre-eminent producer nation. It also wants to take the lead in the production of advanced technologies. The U.S. would like to retain the lead, but our economy is oriented to consumption rather than production.

Deep down inside the cerebral cortex of our national consciousness we assume that the basic purpose of an economy is to provide more opportunities to consume. We grudgingly support government efforts to rebuild our infrastructure. We want our companies to invest in new equipment and technologies but also want them to pay generous dividends. We approve of government investments in basic research and development, but mainly for the purpose of making the nation more secure through advanced military technologies. (We regard spillovers to the private sector as incidental.)

China's industrial and technological policy is unapologetically direct. It especially wants America's know-how, and the best way to capture knowhow is to get it firsthand. So China continues to condition many sales by U.S. and foreign companies on production in China—often in joint ventures with Chinese companies.

American firms are now helping China build a "smart" infrastructure, tackle pollution with clean technologies, develop a new generation of photovoltaics and wind turbines, find new applications for nanotechnologies, and build commercial jets and jet engines. GM recently announced it was planning to make a new subcompact in China designed and developed primarily by the Pan-Asia Technical Automotive Center, a joint venture between GM and SAIC Motor in Shanghai. General Electric is producing wind turbine components in China. Earlier this month, Massachusetts-based Evergreen Solar announced it will be moving its solar panel production to China.

The Chinese government also wants to create more jobs in China, and it will continue to rely on exports. Each year, tens of millions of poor Chinese pour into large cities from the countryside in pursuit of better-paying work. If they don't find it, China risks riots and other upheaval. Massive disorder is one of the greatest risks facing China's governing elite. That elite would much rather create export jobs, even at the cost of subsidizing foreign buyers, than allow the yuan to rise and thereby risk job shortages at home. To this extent, China's export policy is really a social policy, designed to maintain order. Despite the Obama administration's entreaties, China will continue to peg the yuan to the dollar—when the dollar drops, selling yuan in the foreign-exchange market and adding to its pile of foreign assets in order to maintain the yuan's fixed relation to the dollar. This is costly to China, of course, but for the purposes of industrial and social policy, China figures the cost is worth it.

Both America and China are capable of producing far more than their own consumers are capable of buying. In the U.S., the root of the problem is a growing share of total income going to the richest Americans, leaving the middle class with relatively less purchasing power unless they go deep into debt. Inequality is also widening in China, but the problem there is a declining share of the fruits of economic growth going to average Chinese and an increasing share going to capital investment.

Both societies are threatened by the disconnect between production and consumption. In China, the threat is civil unrest. In the U.S., it's a prolonged jobs and earnings recession that, when combined with widening inequality, could create political backlash.

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