Box A: The Composition of China's Growth

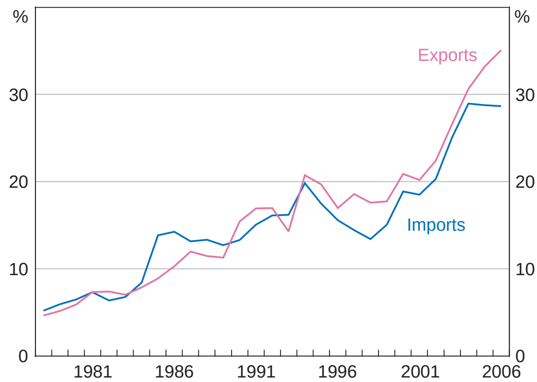
Growth in the Chinese economy has been rapid for an extended period, with annual real GDP growth rising from around 8 per cent to over 11 per cent over the past five years. Continued strong growth has seen China's share of the world economy increase by 3½ percentage points over this period, to 15 per cent in 2006 when measured in purchasing power parity (PPP) terms, with China accounting for around one-quarter of world growth. At market exchange rates, China has increased its share of the world economy by 1½ percentage points over the past five years, to 5½ per cent in 2006 (for a discussion on differences between PPP and market exchange rates, see 'Box A: Measuring Global Growth' in the August 2007 *Statement*). Notwithstanding this performance, China's level of GDP per capita is still comparatively low by world standards – about US$8 000 in PPP terms or around one-fifth of the level in the United States – and most forecasters are expecting further rapid growth in the Chinese economy for an extended period of time.

China's economy has a large and rapidly growing traded sector compared with other major economies. The value of exports has grown by around 30 per cent a year over the past five years, and exports accounted for around 35 per cent of GDP in 2006 (Graph A1). Much of this reflects growth in the processing of goods that have been imported from other countries, particularly east Asia: imports have grown at an annual pace of around 25 per cent over the same period, and are now around 30 per cent of GDP. Nonetheless, the domestic value-added component of recent exports has been rising over time, and much of the growth in imports is for domestic use.

Graph A1

China – Trade

Share of nominal GDP



Source: CEIC

Despite the large traded sector, the expansion of domestic demand has accounted for much of China's recent growth.[1] GDP component data – which are only available in nominal terms – show that domestic demand grew at an annual rate of 14 per cent over the past five years compared with growth of 15 per cent in nominal GDP over this period. More specifically, annual investment growth averaged 19 per cent over this period, and investment is estimated to

1 *In a technical sense, net exports accounted for only around 15 per cent of the increase in China's GDP over the past five years, leaving the bulk of the contribution to growth due to the increase in domestic consumption and investment.*

now account for around 40 per cent of nominal GDP. Household consumption has also been growing strongly, averaging around 10 per cent over the same period, although its share in nominal GDP has declined over time given the rapid pace of investment spending.

The growth in investment appears to be quite broad-based. Not surprisingly, a significant component has been in manufacturing. However, much of the growth has also been development-related, such as the building of extensive subway systems and inter-provincial highways. Notwithstanding the limited quality of the data, the urban fixed-asset investment survey (which measures spending rather than value-added) suggests that around one-quarter of investment has been on infrastructure, utilities and water & environmental management; the real estate category, which includes housing construction (and the purchase of land) accounted for an additional one-quarter (Table A1). This investment has been both a consequence of, and a reason for, the rapid increase in urbanisation in China; the urban population has increased to 44 per cent of the total, up from 30 per cent a decade ago. Given the ongoing large population movements, infrastructure needs seem likely to remain strong in the period ahead.

Table A1: Urban Fixed-asset Investment Expenditure in China

Per cent of GDP

	2004	2006
Total[(a)]	37	42
Of which:		
Primary industry	1	1
Secondary industry	14	18
– Manufacturing	9	12
– Utilities	3	4
– Other	2	2
Tertiary industry	22	24
– Real estate	9	10
– Infrastructure	4	5
– Water & environmental management	3	3
– Other	6	6

(a) Includes land sales

Source: CEIC

China's growth in general, and infrastructure spending in particular, has been resource-intensive. Over the past five years, China has accounted for most of the growth in the world's production of steel and now accounts for around one-third of world steel production. China has also been a large producer of electricity, and accounted for 17 per cent of world electricity production in 2005, up from 10 per cent a decade ago; China's coal-fired power generating capacity is now increasing each year by around the size of the entire British electricity grid. This growth has substantially added to world demand for resources, which has put upward pressure on commodity prices. China now accounts for around 40 per cent of world iron ore imports, between 10 and 20 per cent of copper and nickel imports and 4 per cent of coal imports[2] (Table A2). This demand has been a major benefit to commodity exporters like Australia, where iron ore and coal are the two largest exports, and explains much of the growing importance of China in Australia's export share over the past five years (for further details, see 'Box A: The Changing Country Composition of Australia's Trade' in the November 2006 *Statement*).

2 *Despite producing a large amount of coal, China became a net importer of coal this year.*

Table A2: China's Production and Imports

Per cent

	Share of world		Annual growth
	2001	2006	2006
Production			
Steel	17	35	20
Electricity	12	17[a]	13[a]
Aluminium	14	28	20
Imports			
Coal	1	4	46
Copper	12	12	–32
Iron ore	18	41	19
Nickel	5	22	8

(a) Data for 2005

Sources: ABARE; AME Mineral Economics; International Aluminium Institute; International Iron and Steel Institute; Customs General Administration; CEIC; Energy Information Administration; RBA

The financial sector turbulence associated with the US housing market and the subsequent re-pricing of risk and tightening of credit markets globally appear to have had little direct impact on China's economy to date. This reflects both the large level of saving in China relative to its investment – and hence its large current account surplus – and the relatively closed nature of some Chinese financial markets. Nonetheless, slower GDP growth in the major developed economies would be expected to have some impact on Chinese growth via trade linkages, and IMF forecasts for China have been revised down by ½ percentage point in light of these concerns. However, growth is still projected to be very strong, at around 10 per cent in 2008.