SMU POLITICAL ECONOMIC EXCHANGE

A SMU ECONOMICS INTELLIGENCE CLUB PUBLICATION

This issue in brief:

Greece: At its crossroads after the financial crisis

Greece's economic crisis seems to be of a never-ending nature. In his article, Alton Chen reiterates the causes of Greece's abysmal financial state, and the way forward for the troubled Hellenic Republic.

Oil, its outlook and impact on the financial markets

As of late, oil prices have been plummeting, driving producers and world leaders into a panicked frenzy. Fred Tun's article is a slightly more positive outlook on the dreary oil scenario.

One Child Policy: A Comprehensive Report

Given China's recent abolishment of is long standing One Child policy, several changes are expected to take place. In contrast to the detrimental policy which fined couples for having more than one child, what good can doing away with the policy bring about? Join Zhiyan Jin as she delves further into the issue.

GREECE– AT ITS CROSSROADS AFTER THE FINANCIAL CRISIS

By Alton Chen

Introduction

After Greece officially joined the Eurozone, it borrowed money from the Eurozone and landed itself into debt which it could not repay over the years. Greece was holding on to Euros-denominated debt in addition to its own currency.

Main Causes of Financial Crisis

A significant factor of the financial crisis was Greece's low international competitiveness due to a low labour productivity. Greece used a debt-financed expansionary fiscal policy to raise its average wage level without improving its labour productivity. As a result of higher taxation rates and salaries, Greece became an unattractive manufacturing location for foreign companies. Although Greece was a strong player in the sea shipping industry, the Greek population did not benefit when the industry flourished. Around 10,000 out of 14,000 Greek seamen are currently unemployed because the vast majority of Greek ship-owners decided to sail under foreign flags to reduce its operational costs (Paris, C., 2015).

The second reason which resulted in the financial crisis was Greece's intense deficit spending. Before the Euro existed, the Greek government had to pay high interest rates on its loans. After entering the Eurozone in 2001, Greece was able to pay considerably lower interest rates since it was backed by strong economies like Germany. Hence, the Greek government started borrowing more money to garner voters by fostering consumption via newly created jobs, increased pension funds and salaries. For instance, 17.5% was spent of Greece's economic output on pension funds, which was above the average of 13.2% in European Union (EU) (BBC News, 2015). Since the 2008 Global Financial Crisis, Greece could not obtain any new loans from financial institutions to pay off its old debt, which led to a crisis (Kolivakis, L., n.d.). Germany and other Eurozone members thus had to intervene to save Greece from bankruptcy.

The last reason is which prevented Greece from increasing its productivity, was nepotism. Three families, Mitsotakis, Papandreou and Karamanlis have been in charge of the Greek government since the end of World War II till 2015 (Lopez, L., 2015). They have rewarded fellow party members for their loyalty by giving them jobs in public service, which created an incompetent and expensive public administration to hinder any reform policies from taking place.

Effects of Crisis

As part of the first two bailout packages, Greece implemented austerity measures in exchange for financial assistance, including reduced spending and higher wages. This strained the Greece's economy as there were more people driven to poverty, and millions lost jobs or had reduced salaries. Most middle class workers either lost their jobs or were forced to accept a lower salary for doing the same amount of work. Around 1.27 million Greeks were unemployed in 2014, with those unemployed between aged 15 years to 29 years increasing from 16.2% in 2008 to 45.0% in 2014 (Hellenic Statistical Authority, 2015). As seen in Figure 1, Greece's Gross Domestic Product (GDP) has decreased by 33.5% from USD354.62 billion in 2008 to USD235.57 billion in 2014 (Hellenic Statistical Authority, 2015).

Figure 1: Greece's Gross Domestic Product (GDP) Source: Tradingeconomics.com (2015)

Although debt levels only increased slightly, a larger decrease in GDP caused debt to GDP ratio to worsen, which reached its highest of 177% in 2014 (Hellenic Statistical Authority, 2015). This indicated Greece's inability to service its debts, which was detrimental for its future economic outlook.

Both economic and employment insecurity impacted many Greece's households. Furthermore, 93.1% of Greek households encountered a significant reduction in their income between 2010 and 2013 (IME GSEVEE, 2013). There was at least one unemployed member in at least 40% of the households because they could not afford the increased living costs (IME GSEVEE, 2013). Commonly used drugs became inaccessible because there was a shortage of public drugs (Brozak, S., 2015). Likewise, the lower income faced difficulties to survive because austerity measures has reduced the financial assistance they received further.

Greece also faced political instability due to the financial crisis, which is evident from a drop in Greece's political stability index from 0.53 in 2007 to 0.02 in 2014 (Worldwide Governance Indicators, 2015). This was attributed to a succession of Greek governments over the past five years, George Papandreou's centre-left PASOK government, Lucas Papdemos's technocratic government, Antonis Samara's centre-right New Democracy government and Alexis Tsipras's far-left Syriza government (Lachman, D., 2015). A lack of political consensus to handle the financial crisis has only created more anxiety among voters, which contributed negatively to Greece's road to recovery. Since the Syriza-led government took over in January 2015, bank deposits have dropped substantially in the subsequent months (W, P., 2015).

Figure 2: Drop in Greece's bank deposits Source: Economist.com

Solutions

A possibility was for Greece to exit the Eurozone and to default on its debts. Greece would have then recovered through the use of its own independent monetary policy. However, it appeared that a Greece exit was unpopular among the Eurozone and Greece population (The Economist, 2015). This would result in a fall in asset prices due to a wipe-out of wealth in Greece. This would impede European integration and possibly encourage other countries to follow suit.

Next, Greece could have also considered boosting its competitiveness by lowering its real exchange rate. This can be done by reducing prices of Greece's domestic goods, by privatisation of Greece's state-owned assets and liberalisation of its labour markets. This would have led to reduced domestic prices, which improve competitiveness and efficiency so that Greece would have more national income (Rankin, J., & Smith, H., 2015).

Lastly, a trimming of Greece's debt was recommended by International Monetary Fund's (IMF) new chief economist, Maurie Obstfeld. This was likely to be mandatory because a haircut of €107 billion made from Greece's private creditors in the 2012 debt restructuring had been unsuccessful (Spence, P., & Chan, S. P., 2015). As part of Greece's third bailout conditions, it needed to make reforms to their generous pension system, which had already suffered under previous bailouts (The China Post, 2015). The German chancellor, Angela Merkel, has also suggested debt restructuring through lower interests rates and extended loan maturity (Spence, P., & Chan, S. P., 2015).

Current outlook

As IMF requires the EU to provide significant debt relief for Greece, plans for future debt restructuring talks would likely determine Greece's future road to recovery (Elliott, L., Wearden, G., & Treanor., 2016). However, it remains to be seen whether Greece would succeed even with future reform measures and better debt conditions.

References

1. BBC News, (2015, July 3). *The cost to pensioners.* Retrieved 15 December 2015, from http://www.bbc.com/news/world-europe-33382046
2. Brozak, S. (2015, July 15). Greece Is On The Verge Of A Health Catastrophe. Retrieved December 17, 2015, from http://www.forbes.com/sites/stephenbrozak/2015/07/15/greece-medical-collapse/#68c4717512b1
3. Elliott, L., Wearden, G., & Treanor, J. (2016, January 21). On the Greek road to political instability. Retrieved January 24, 2016, from http://www.theguardian.com/business/2016/jan/21/imf-demands-debt-relief-from-europe-for-greece-before-new-bailout
4. Hellenic Statistical Authority, (2015, December 30). Greece In Figures, October – December 2015. Retrieved January 10, 2016, from http://www.statistics.gr/documents/20181/1515741/GreeceInFigures_2015Q4_EN.pdf/681d9d6b-6636-4163-927a-a18c81ce39d1
5. IME GSEVEE, (2013, February 8). Survey by IME GSEVEE - "Income - Expenses of households." Retrieved December 23, 2015, from http://www.imegsevee.gr/pressrelease/601-survey-by-ime-gsevee-qincome-expenses-of-householdsq
6. Kolivakis, L. (n.d.). Greece's Pension Paradox? Retrieved 14 December 2015, from http://pension360.org/greeces-pension-paradox/
7. Lachman, D. (2015, September 18). On the Greek road to political instability. Retrieved January 4, 2016, from https://www.aei.org/publication/on-the-greek-road-to-political-instability/
8. Lopez, L. (2015, February 8). The Political Dynasties That Destroyed Greece, And The Real Reason The Country Is Such A Mess. Retrieved December 28, 2015, from http://www.businessinsider.com/greeces-political-dynasties-the-reason-for-the-crises-2011-7?IR=T&r=US&IR=T
9. Paris, C. (2015, September 9). Greek Shipowners Prepare to Weigh Anchor on Prospect of Higher Taxes. Retrieved December 20, 2015, from http://www.wsj.com/articles/greek-shipowners-prepare-to-weigh-anchor-on-prospect-of-higher-taxes-1443520314

10. Rankin, J., & Smith, H. (2015, July 24). The great Greece fire sale. Retrieved January 5, 2016, from http://www.theguardian.com/business/2015/jul/24/greek-debt-crisis-great-greece-fire-sale
11. The China Post, (2015, July 15). A closer look at the punishing terms of the Greek bailout deal. Retrieved 20 December 2015, from http://www.chinapost.com.tw/international/europe/2015/07/15/440667/A-closer.htm
12. The Economist, (2015, July 4). Europe's future in Greece's hands. Retrieved 18 December 2015, from http://www.economist.com/news/leaders/21656662-whatever-its-outcome-greek-crisis-will-change-eu-ever-europes-future-greeces
13. Tradingeconomics.com. (2015). Greece GDP| 2006-2014 | Data | Chart | Calendar | Forecast | News. Retrieved 28 December 2015, from http://www.tradingeconomics.com/greece/gdp
14. W, P. (2015, June 28). The referendum and Greek Banks. Nowhere to get money. Retrieved December 22, 2015, from http://www.economist.com/blogs/freeexchange/2015/06/referendum-and-greek-banks
15. Worldwide Governance Indicators. (2015). WGI 2015 Interactive. Retrieved December 30, 2015, from http://info.worldbank.org/governance/wgi/index.aspx#doc

OIL PRICES, ITS OUTLOOK AND IMPACT ON FINANCIAL MARKETS

by Fred Tun Lin Win

Source: Shutterstock

Causes of fall in oil prices

In recent months, oil prices have fallen to a record low, far below the $30/barrel mark. This recent drastic fall in oil prices boils down to the basic concept of supply and demand.
On the supply side, USA overtook Saudi and Russia to become the largest producer of oil in the world, with daily output exceeding 11 million barrels in the first quarter of last year (Smith, 2014). In response to this increase in supply of oil from the US, Saudi Arabia pushed for OPEC to up their supply of oil, hoping to maintain their market share instead of reducing their output.

The rationale of the decision was simple; the Saudis wanted to engage in a price war against the US in an oversupplied market. They wish for US shale frackers to be eventually be driven out of business due to their higher operating costs. As of Dec 4 2015, OPEC members could not reach an agreement to curb the production of oil and announced that it would abandon the 30 million barrels per day limit (Hurst, Razzouk & Lee, 2015). This oversupply is likely to continue as only recently were the sanctions on Iran lifted, following which Iran announced an increase in production to as much as 4 million barrels a day by the end of 2016, up from their current rate of about 3.3 million barrels a day. All this has led to an oversupply of the oil, thus causing the plummeting oil prices.

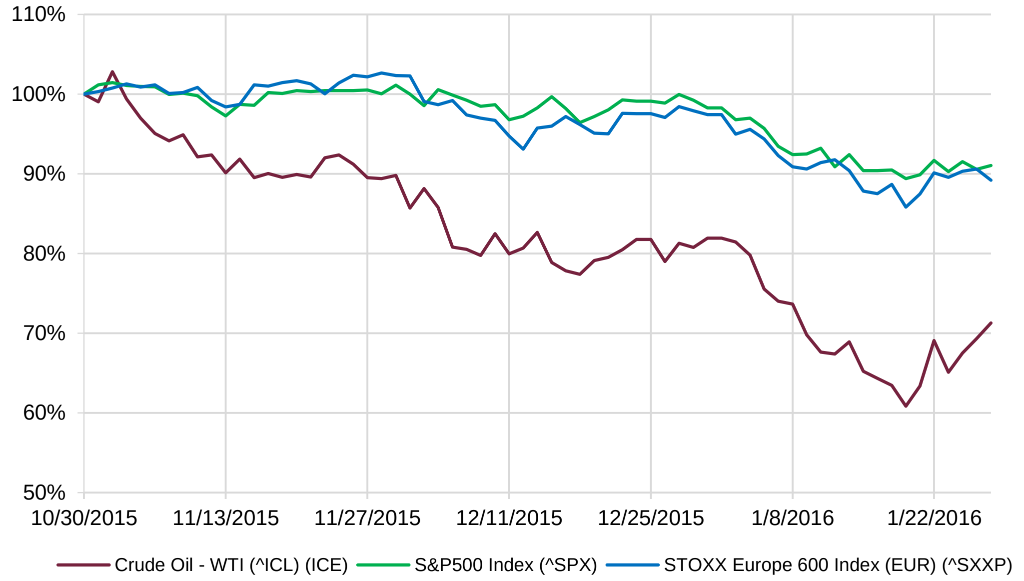
On the demand side, China's traditional sector of heavy industry and production has been shrinking over the past months and is expected to continue in the same trend (Watts & Hsu, 2015). As China is the largest importer of oil in the world and manufacturing is highly energy intensive, there is a significant decrease in the demand for oil, thus further driving prices lower. And China is not alone as US manufacturing has also fallen, thus contributing to the lower prices of oil.

Effects of fall in oil prices

The effects of the fall in oil prices are evident on the consumer level. Gasoline prices at gas stations and pumps are now cheaper. Households that use heating oil for warmth are reaping the benefits of lower prices. Net importers of oil such as the US and China are also benefitting from the lower prices as a result of cheaper inputs. However, the oversupply of oil has increased pressure on the poorer OPEC members such as Venezuela, Nigeria and Ecuador, who are heavily reliant on their oil exports. These countries have suffered significantly as the low prices have been cutting into their profits (Brindicci, 2016). Many oil producing companies have also seen significant chunks of their market capitalisation being wiped out as a result of the plunging prices. For instance, ExxonMobil and PetroChina Co. lost $11 billion and $16 billion of their value respectively, after the Dec 4 OPEC meeting (Katakey, 2015). There have also been significant layoffs in the oil industry, with an estimated 250,000 jobs cut worldwide since the decline in prices (Reed, 2016).

Outlook of oil & Impact on financial markets

WTI climbed 9% (Saefong, Kantchev & Hsu, 2016) to $32 per barrel after ECB President Mario Draghi hinted at easing measures to steady inflation, signalling greater investor confidence. On the same day, stocks also rallied, with S&P500 climbing 2% and Stoxx Europe 600 climbing 3% (Mozee, 2016). It is now an environment where oil, instead of economic fundamentals, is driving sentiment and as a result stocks appear highly correlated to oil prices, as shown in the graph below.



Source: S&P Capital IQ

For the financial market to separate itself from oil prices, investors will have to focus on economic fundamentals again, for which oil prices will need to stabilise. However, in the short term, oil prices are unlikely to stabilise, as stated in a report by EIA, signalling an increase in supply. While there has been a slight decrease in operating rig counts and decreasing production in Texas, production is not expected to decrease significantly in the short term. Therefore, some analysts still expect oil prices to fall as low as $20 per barrel before any significant rebound is going to take place. Additionally, the nature of drilled-but-uncompleted (DUC) wells is such that they require relatively low capital for the rigs to be brought online in a short period of time. Therefore, US shale producers can simply wait on the DUCs for oil prices to rise and then resume pumping oil which would result in further fluctuations in the oil prices in the short term.

However, in the long term, oil prices should stabilise as many of the operationally inefficient producers are forced out of the market. Many of the shale oil producers were not cash flow positive even when oil was priced at $100 per barrel. The only reason why shale is still surviving is due to existing hedges and patience from creditors, which will not last forever. Therefore, once the inefficient shale oil producers are forced out of the market eventually, oil prices and the financial markets will stabilise.

The short term volatility of oil is also unlikely to hamper the recovery of the global economy from the recession. Janet Yellen's decision to raise of interest rates by 25 base points in December last year is a signal of confidence that the falling oil prices will not have a significant impact on the US economic outlook, since the 2% inflation target would be met once oil prices stabilise.

As for the Eurozone, Draghi sees the falling oil prices as a cause for concern and that "the fall in oil prices could feed into the prices of other goods, contributing to a downward, deflationary spiral" (Watts, 2016). However, the possibility of an ECB stimulus in March could help the Eurozone avoid a recession if oil prices do remain at its current levels. Only China is presently seeing a slowdown in growth which is a cause for concern as it may lead to further fall in oil prices. Even so, the slowing of the Chinese economy has a relatively smaller impact than the oversupply of oil that is flooding the market. Additionally, as the largest net-importer of oil in the world, the low oil prices will help downstream players and help manufacturing industries lower their inputs.

Conclusion

In conclusion, the current low price of oil is unlikely to hamper the road to recovery for the US and Eurozone, as it is simply an issue of oversupply, not slowing demand in these countries. Additionally, the current situation is beneficial to the economies of net importing countries and the financial markets will also stabilise with oil prices once the less efficient shale producers are forced out of the market.

References

1. Brindicci, M. (2016, January 20). Ecuador president says he's tired of fighting with OPEC. Retrieved January 28, 2016, from http://www.reuters.com/article/us-ecuador-opec-idUSKCN0UY2GK
2. Hurst, L., Razzouk, N., & Lee, J. (2015, December 5). OPEC Unity Shattered as Saudi-Led Policy Leads to No Limits. Retrieved January 28, 2016, from http://www.bloomberg.com/news/articles/2015-12-04/opec-unity-shattered-as-saudi-led-policy-leads-to-no-limits-ihs9xu51
3. Katakey, R. (2015, December 11). Oil Investors Are $240 Billion Poorer a Week After OPEC Call. Retrieved January 28, 2016, from http://www.bloomberg.com/news/articles/2015-12-11/oil-investors-are-230-billion-poorer-a-week-after-opec-decision
4. Mozee, C. (2016, January 22). European stocks gain most in nearly 4 months on QE hopes, oil spike. Retrieved January 28, 2016, from http://www.marketwatch.com/story/european-stocks-set-to-break-weekly-losing-streak-on-ecb-stimulus-hopes-2016-01-22?siteid=nwteurope1/22/2016
5. Reed, S. (2016, January 12). Stung by Low Oil Prices, BP Will Cut 4,000 Jobs. Retrieved January 28, 2016, from http://www.nytimes.com/2016/01/13/business/energy-environment/bp-jobs-oil-prices.html?_r=0?register
6. Saefong, M., Kantchev, G., & Hsu, J. (2016, January 22). WTI oil soars 9% to settle at a two-week high. Retrieved January 28, 2016, from http://www.marketwatch.com/story/oil-prices-rip-higher-after-ecb-stimulus-promise-echoes-2016-01-22?siteid=nwtasiadaily
7. Smith, G. (2014, July 4). U.S. Seen as Biggest Oil Producer After Overtaking Saudi. Retrieved January 28, 2016, from http://www.bloomberg.com/news/articles/2014-07-04/u-s-seen-as-biggest-oil-producer-after-overtaking-saudi
8. Watts, W., & Hsu, J. (2015, November 2). Oil ends lower on weak China data, record Russian crude production. Retrieved January 28, 2016, from http://www.marketwatch.com/story/oil-prices-sluggish-after-china-manufacturing-data-2015-11-02
9. Watts, W. (2016, January 21). 4 key takeaways from Draghi's 'no limits' statement. Retrieved January 28, 2016, from http://www.marketwatch.com/story/4-key-takeaways-from-draghis-no-limits-statement-2016-01-21

CHINA'S ONE-CHILD POLICY: A COMPREHENSIVE REPORT

By Zhiyan Jin

Introduction

On 29th October 2015, China's National People's Congress Standing Committee decided to overturn its 36-year-old one-child policy, with the state advocating couples to have 2 children instead, coming into effect on Jan 1, 2016[i]. It was hailed as a big move to balance gender ratios and continue to power the development of the national economic engine. This report seeks to give a comprehensive coverage of the policy's background, and its economic and social consequences that led to abolishment. It also seeks to weigh whether the relaxation has come too late and will be rendered helplessly ineffective.

Historical Background

China's one-child policy as a population control mechanism was officially instituted in 1979 as a major reversal of the 1960s call to have as many children as possible, and has since been managed by the notorious National Family and Population Planning Commission since 1981, bringing official tallies and administration under official control[ii]. It has been relaxed over the years due to special considerations: All non Han-majority Chinese were allowed to have 2 children if they lived in urban areas, and 3-4 children if they lived in rural areas. Rural Han Chinese were also allowed a second child if their first child was a girl. (ref: guardian article – china's great gender crisis)In 2013, following the Third Plenum of the Chinese Communist Party, the policy was also relaxed for all couples if one of them was an only child[iii]. The one-child policy has been notorious for causing innumerable infant and foetal deaths and shaping unhealthy societal practices, creating unbearable economic pressures that weigh on the single-children; numerous demographic figures also paint a depressing economic outlook for the long run.

Problems Caused & Reasons For Abolishment

a) Economic reason

Human capital is one of the four major ingredients of economic growth, one which China is now sorely lacking. It faces a future as an ageing economy, possibly "getting old before getting rich"[iv], bucking the trend of other economies like Europe or Japan. China's fertility rate has fallen sharply due to strict enforcement of the policy such as forcible late abortions and extravagant penalty costs of having a second child, as well as economic pressures which compounded it; According to World Bank data, its fertility rate has fallen from 2.7 in 1981 to

1.7 in 2015[v]. Previously in the 1960s and early 1970s, fertility rates were estimated at over 5, due to Mao's call for having more children that tied in with political and economic doctrines[vi]. Refer to Figure 1 below for an illustration of the decline over the years. According to a UN paper[vii], China's median age in 1980 was 23.7, but has risen to 37.0 in 2015, and is projected to surge to 49.6 by 2050 if current trends continue. Official estimates state that there have been around 400million prevented births due to the policy[i], but positive estimates are that only 30 million new births will be added by 2050[viii]; the UN and the Population Reference Bureau suggest that the abolishment will add about 23.4 million extra people instead.

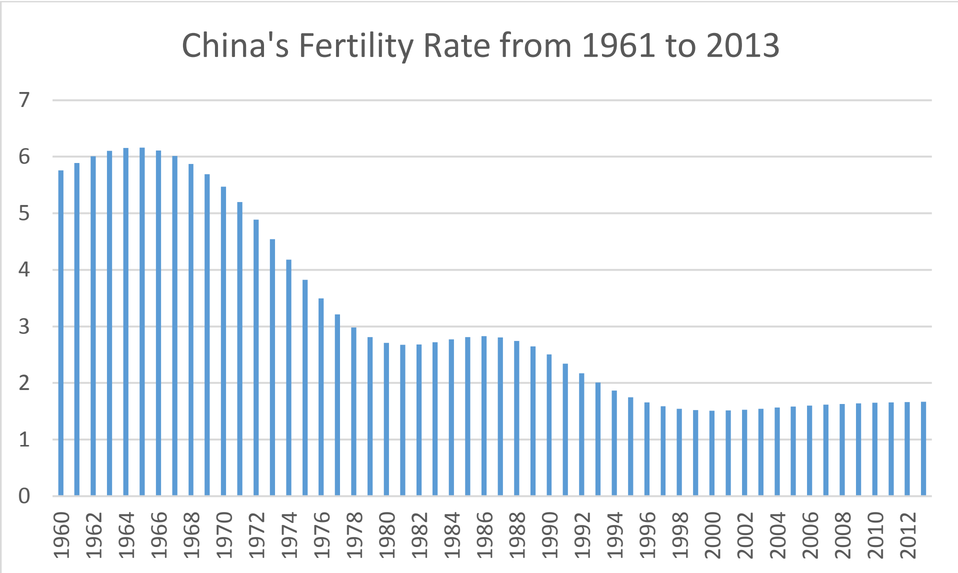


Figure 1: China's Fertility Rate from1961 to 2013
Source of data: All Countries' Fertility Rate Data from World Bank
Figure 1 is self-generated from China's data from 1961 to 2013

The economic reasoning behind the policy abolishment is simple: Human capital is a raw material for production and one especially important to China, where the combined agriculture and industry share of GDP is over 50%[ix]. As the population ages, working age population, defined officially as those aged 16 to 59, will shrink, leading to a resource crunch, which ups the salary due to shortage of labour and hence unit cost of human capital. Companies act rationally to maximize profits: As the unit cost of human capital rises, cost of production for unit of goods or services rises and the companies may turn to automation[x], force workers to work more for the same pay, or shift away from China as base of production. In reality, data presented is probably already too rosy: China begins tallying the working age population at 16, but many of these young persons are still full-time students who contribute little if at all to the total workforce. Also, there are a number of under-60 persons who have retired early and depend on their spouse. As China's working age population is projected to fall 10% by 2040[xi], these shifts are becoming increasingly viable options. The rise in production costs and possible shift elsewhere can only hurt China's economy, which remains industry-centric. The National Health and Family Planning Commission vice minister has said that the abolishment is expected to boost the country's economic growth rate by about 0.5% stemming from the work force increase[viii].

The next economic reason would be the burden placed on the government and economy by the rise in number of retired pensioners paired with the fall in tax contributing base. China has in place a 3-part pension system: for rural residents, urban residents, and certain company pension systems. The rural pension system which covers over 500 million persons pays out between 100-500 RMM to pensioners a month, the urban system covers 320 million with 80 million receiving and 240 million contributing, and pays out an average of 2100 yuan to each receiver monthly. Some companies also have company pension systems which are voluntary and managed by the companies themselves[xii]. As China's standard of living increased exponentially following its opening up to global economic trade, quality of life and standard of life have increased, and lifespans have grown from under 45 before the 1950s to over 75 today[xii].

Meanwhile, as the benefitting pool is increasing due to the ageing society, the workforce who can work and contribute are being greatly reduced. The pension systems are generous but have not kept up with changing times, and weigh as a huge burden to Government finances. It would be greatly beneficial in the coming decades to increase the number of births, to increase the support ratio and relieve the stress on government finances. While the proportion of China's population over 65 was 9% in 2014, it is predicted to rise to 24% by 2050. This puts it as one of the fastest ageing economies in the world, as illustrated in Figure 2. A report published by the Chinese Academy of Social Studies reported that without adjustments, pension deficits would begin in 2030[xiii]. Hence, there is a pressing need to increase the number of births to widen the pool of contributors and relieve government burden.

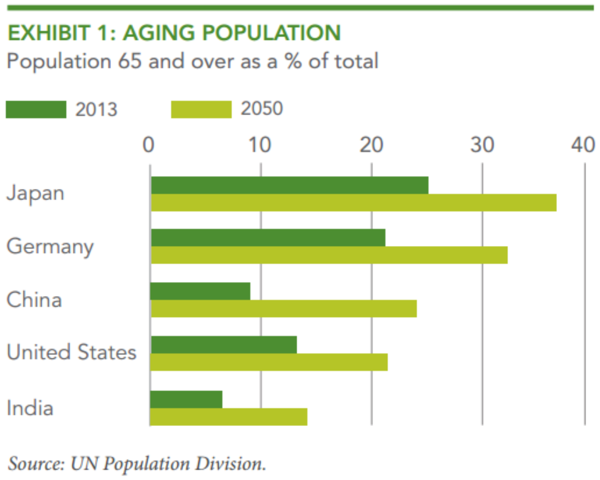


Figure 2: Current and Projected Percentages of Population over 65 for Some Major Economies
Source: Paper: China's Retirement System: What does The Future Hold
Retrieved from https://us.dimensional.com/media/323321/Chinas-Retirement-System-What-Does-the-Future-Hold.pdf

b) Societal Reason

As the policy took shape over 30 years and quality of life has risen, it has resulted in increasingly smaller families with more vertical family ties than horizontal. This means that there are more generations living together due to longer lifespans, but less number of members in each new generation. Now, the most common form of family support is the 4-2-1 ratio, where 4 grandparents are supported by 2 parents, in turn supported by the single child when he or she matures[xiv]. This has created enormous pressures for the children to live up to: what filial duties which used to be shared by 2-3 children or more now depend solely on the single child to fulfil. Besides the funneling of responsibility, filial piety is yet another reason this cannot be circumvented – traditional Confucian values teach that the most important value any person can hold is filial piety, to respect and support the parents and elders who have nurtured you. China's laws such as the Criminal Law of 1979 also state that children may be fined and jailed for refusing to support an elderly family member[xv]. The pressure on the children is huge and has probed a societal discussion and review into how the society can function to stem this depressing trend. Hence, the abolishment of the one-child policy is seen as the best way to buck the trend and alleviate pressures on the younger generation while still maintaining that responsibility for the aged falls primarily on their descendants and not the government.

The last problem caused by the one-child policy is gender imbalance and its consequent effects. The birth rate for boys is naturally higher than for girls, at around 103-107:100. China traditionally favours boys over girls, because boys are seen as being able to “carry on the family line” and retain the family name, as well as being more dependable because of their size physical ability and not needing to “marry into another family”. With improvements in sex-identifying technology to reveal the fetus’ gender before birth, it has become easier to manipulate birth ratios. Increasingly accessible and easily-carried-out sex-selective abortion have skewed the sex-ratio even more drastically, to 120-130:100 across different provinces[xvi]. But this promises devastating consequences, as it has been calculated that by 2020, there will 30 million men of marriageable age unable to find a spouse because there are simply not enough women, possibly leading to societal instability[xvii]. Also, with the shortage of marriageable women, there are evermore pressures on needed on the men before their prospective in-laws deem them worthy of their daughters – they are frequently expected to own a house of their own – a particularly difficult task, given the high property prices in cities[xviii]

Will it help or not?

The abolishment is expected to add 30 million people to the workforce by 2050, but experts expect a smaller number[i]. This section will analyse the effectiveness of the policy in the economic and societal aspects.

Economic Effects

It is expected that with the abolishment of the one-child policy, fertility rates will be boosted, leading to higher expenditure by couples. There are two pathways by which this will be a boon to the economy: the increase in household spending, as well as the fall in aggregate savings rate.

Firstly, with more families having two children rather than one, families’ spending will have no choice but to increase. Although in some sectors, there will be less increase spending, for example when the younger child receives hand-me-downs from the older child instead of buying brand new ones; there will be a definite boost in other sectors like necessities and education. Education is a particularly hot industry in China as the previous one-child policy has created a fanatical race-to-the-top with education sitting at the pinnacle[xix]. Academic competition has spurred the booming tuition industry as well as early childhood education programs and complementary products. And as this generation ages, demand for necessities, housing, consumer and lifestyle products and ageing products will also increase correspondingly. The increase in number of children will thus fuel an increase in domestic consumption driven by household consumption and trigger the multiplier effect (China’s multiplier is roughly 2), leading to rise in the GDP. Also, as these babies age, they add to the human capital of economic growth, fueling both supply and demand in the Chinese economy.

Secondly, the aggregate savings rate will fall with couples having two children. Asian savings rates are exceptionally high and China is a prime example: its gross savings rate in 2013 was 50% of GDP[xx], as compared to the United States which had 18% or India with 32% (the exact same reference). In 2009, urban households with 2 children saved 12.8% of their incomes while those with 1 saved 21.3%, and this difference remains large across different income ranges[xix.] In urban families with twins from 1992-2009, with each additional child (usually the twin), the family's savings rate fell by 6-7%[xxi]. The high savings rate has been attributed to historical reasons, precautionary savings[xxii], demographic reasons because the huge baby-boomer population saves aggressively for retirement, as well as pressures on both parents and children to save as a result of the one-child policy[xxiii].

Economic theory prescribes that the national savings rate is positively correlated with economic growth as savings provides the needed capital for investments. China already has dangerously high investment levels[xxiv] and more-than-sufficient savings which are locked in savings accounts and could be better directed elsewhere. China's economy needs to transit from the unstable and excessive investment-driven economy to a domestic consumption-driven economy. And to do that, capital needs to be directed from being locked excessively and uselessly in savings accounts to being pumped into the economy through domestic consumption, to fuel GDP growth.
The abolishment will definitely improve the economy – the question is by how much. While the growth in sectors like housing and necessities is guaranteed by the rise in population, the extent of other sectors' increases depend substantially on the people's attitude towards consumption – how willing they are to fork out additional extravagant amounts for the second child as is being done for the single child. The diverting of savings also remains to be seen. We can only bank on the empirical minimum of 6-7% decline, given that China has its uniquely strong army of reasons for the high savings rates.

Social Effects

The abolishment is expected to be less than effective in alleviating the social problems. After media release of the news, popular networking and news site Sina.com ran a poll of over 120,000 Chinese and found that 40.5% of respondents will not have a second child and 29.1% said they will make a decision after weighing the family and economic situation[xxv]. Commonly cited reasons were the cost of raising a child, health reasons, and the abolishment coming too late.

Although the official data estimates than around 30 million newborns will be added, experts say that the reality will be less positive due primarily to economic and financial reasons - the cost of raising a child is simply too high. According to a 2003 study by the Shanghai Academy of Social Sciences, it takes 490,000 RMB to raise a child to 16 years old in Shanghai, meaning that average families will spend 40-50% of their income on the child's expenses alone[xxvi]. Although the study was not wide enough to take into account other regions in China, the figure provides an indicator of the expensive situation.

Another reason is the health of prospective parents-to-be. While China has become economically prosperous, a visible and critical trade-off has been the environment and health of the people. According to the China Population Association, the percentage of infertile women who are of child-bearing age jumped from 3% in 2002 to 12.5% in 2012. While there is no evidence to shine light on the cause, the pollution of the environment as well as later child-birth are thought to be leading causes[xxvii]. After the abolishment, many parents also lamented that while they would like to have a second child, they regret that they are already past their youthful years and fear that they are no longer able to take care of a young child, and so will not take up the two-child policy.

So, although there will be a definite uptick in the economy stemming from the policy change, it does not do enough to reverse the tide of gender selection and unbalanced sex ratios leading to societal instability across the country. Having more children does not equate to having more fair and balanced sex ratios, free of traditional bias. However, it is likely that the abolishment will alleviate the 4-2-1 support ratio in those families who do choose to take it up. Hence, the societal impact will be limited but visible.

Conclusion

Well-meaning and designed policies failing retrospectively are but a dime a dozen. While the One-Child Policy was an era of oppression and perhaps excess intervention, the abolishment now offers the Chinese more freedom and choice of family structure and division of familial responsibilities. Hopefully this will spur a move in the right direction for societal and gender ratios, even though current views present that as less than rosy. National economies never fail without bringing great turmoil, what's more China, as the second-largest economy in the world. The government would do well to rethink more past policies and pursue growth more aggressively with a view to the future as it ruminates over the past and present.

References:

[i] XINHUA. (2015, December 27.) Chinese bid farewell to one-child policy with law amended. Xinhua News. Retrieved from http://news.xinhuanet.com/english/2015-12/27/c_134956074.htm

[ii] Short, S., Zhai, F. (1998) Looking Locally at China's One-Child Policy. *Studies In Familly Planning, 29, 373-387.* DOI: 10.2307/172250

[iii] Hatton, C. (2013, November 13.) China reforms: One-child policy to be relaxed. *BBC News.* Retrieved from http://www.bbc.com/news/world-asia-china-24957303

[iv] The Economist Special Report. (2009 June 25). China's predicament. *The Economist.* Retrieved from http://www.economist.com/node/13888069

[v] World Bank. (2016) *Fertility rate, total (Births per woman).* Retrieved from http://data.worldbank.org/indicator/SP.DYN.TFRT.IN

[vi] Gerhard, H.K. (2011 June 9). China: Total Fertility: Analyses: Tables, Figures and Maps. Retrieved from http://www.china-profile.com/data/fig_WPP2010_TFR_1.htm

[vii] United Nations. (2015). *World Population Prospects – Key findings & advance table – 2015 Revision.* (Report No. ESA/P/WP.241) Retrieved from http://esa.un.org/unpd/wpp/publications/files/key_findings_wpp_2015.pdf

[viii] Wee, SL. (2015, November 10) China says two-child policy will contribute 0.5 percentage point to growth rate. *Reuters.* Retrieved from http://www.reuters.com/article/us-china-economy-population-idUSKCN0SZ0OK20151110#wDX7ZtM35bjJVaT6.97

[ix] Central Intelligence Agency. (2014.) *The World Factbook. GCP – Composition – By Sector Of Origin.* Retrieved from https://www.cia.gov/library/publications/the-world-factbook/fields/2012.html

[x] Ryan, K. (2015 April 22). The Automation Of China's Labour Force. *China Briefing*. Retrieved from http://www.china-briefing.com/news/2015/04/22/automation-chinas-labor-force.html
[xi] Mitchell, T. (2015, December 9). China working age population 'to fall 10% by 2040. *Financial Times.* Retrieved from http://www.ft.com/intl/cms/s/0/d6681cba-9e3c-11e5-b45d-4812f209f861.html#axzz3xVFA5Zs2
[xii]Peng, Chen. (2015). *China's Retirement System: What Does The Future Hold?* Retrieved from https://us.dimensional.com/media/323321/Chinas-Retirement-System-What-Does-the-Future-Hold.pdf
[xiii] The Economist. (2014 April 5). Paying for the grey. *The Economist.* Retrieved from http://www.economist.com/news/china/21600160-pensions-crisis-looms-china-looks-raising-retirement-age-paying-grey
[xiv] W, F W., & Y Zhang. (2006) Who will care for the elderly in China?: A review of the problems caused by China's one-child policy and their potential solutions. *Journal of Aging Studies,20. 2, 151-164 (PAGE 151-164)* doi:10.1016/j.jaging.2005.07.002
[xv] Michael Palmer (1995). The Re-emergence of Family Law in Post-Mao China: Marriage, Divorce and Reproduction. *The China Quarterly*, 141, pp 110-134. doi:10.1017/S0305741000032938.
[xvi] All Girls Allowed. (2013) *Gender Imbalance In China.* Retrieved from http://www.allgirlsallowed.org/gender-imbalance-china-statistics
[xvii] BBC News. (2007 January 12). Chinese facing shortage of wives. *BBC News.* Retrieved from http://news.bbc.co.uk/2/hi/asia-pacific/6254763.stm
[xviii] Branigan, T. (2011 November 2). China's Great Gender Crisis. *The Guardian.* Retrieved from http://www.theguardian.com/world/2011/nov/02/chinas-great-gender-crisis
[xix] Jin, Keyu. (2016 January 8). China's two-child policy: far-reaching impact. *The Himalayan Times.* Retrieved from http://thehimalayantimes.com/opinion/chinas-two-child-policy-far-reaching-impact/
[xx] World Bank. (2015). *Gross Savings (% of GDP).* Retrieved from http://data.worldbank.org/indicator/NY.GNS.ICTR.ZS
[xxi] Choukhmane,T., & Coeurdacier, N., & Jin, Keyu. (2014). *China's one-child policy and saving puzzle.* Retrieved from http://www.voxeu.org/article/china-s-one-child-policy-and-saving-puzzle
[xxii] Harbaugh, R. (2004). *China's High Savings Rates.* Retrieved from https://kelley.iu.edu/riharbau/harbaugh-chuxu.pdf
[xxiii] Tao, Y D., & Zhang, JS., & Zhou SJ. (2011). *Why Are Savings Rates So High In Chin*a?. NBER (Working Paper 16771) Retrieved from http://www.nber.org/papers/w16771
[xxiv] Lee IH., Liu S., & Syed M. (2012). *Is China Over-Investing and Does It Matter?* IMF Working Paper WP/12/277. Retrieved from https://www.imf.org/external/pubs/ft/wp/2012/wp12277.pdf
[xxv] Fan, H. (2015 October 30). Why China's child policy doesn't add up for its citizens. *CNBC.* Retrieved from http://www.cnbc.com/2015/10/30/why-chinas-child-policy-doesnt-add-up-for-its-citizens.html
[xxvi] China Daily. (2005 April 1). Parents Pay Too Much For Education. *China Org.cn.* Retrieved from http://www.china.org.cn/english/Life/124528.htm
[xxvii] Minter, A. (2015 December 31). China's flirtation with surrogacy, as the one-child policy comes to a close. *The Sydney Morning Herald.* Retrieved from http://www.smh.com.au/comment/chinas-flirtation-with-surrogate-motherhood-as-the-one-child-policy-comes-to-an-end-20151230-glx5hr.html

SEIC Correspondents for Issue 59:

Sreya Sanyal (Director, SPEX)
Undergraduate
School of Business
Singapore Management University
ssanyal.2013@business.smu.edu.sg

Nguyen Duong Thuy Uyen (Creative Director)
Undergraduate
School of Business
Singapore Management University
dtunguyen.2014@business.smu.edu.sg

Alton Chen (Writer)
Undergraduate
School of Accountancy
Singapore Management University
alton.chen.2013@accountancy.smu.edu.sg

Fred Tun Lin Win (Writer)
Undergraduate
School of Business
Singapore Management University
linwin.tun.2014@business.smu.edu.sg

Zhiyan Jin (Writer)
Undergraduate
School of Business
Singapore Management University
zhiyan.jin.2015@business.smu.edu.sg