ICS Conversation

Outlook for the Chinese Economy in the COVID Era

Speakers:

Prof. Chen Zhiwu, Director of AsiaGlobal Institute, Chair Professor of Finance, Victor and William Fung Professor in Economics, The University of Hong Kong.

Prof. Yao Yang, Dean, National School of Development, Director, China Center for Economic Research, Peking University.

Moderator:

Amb. Shyam Saran, Former Foreign Secretary to the Government of India, Member, Governing Council, Institute of Chinese Studies, Delhi.

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Venue: Zoom Webinar

Amb. Shyam Saran initiated the session by raising a question to Prof. Yao Yang with respect to the current situation of the Chinese economy. Stating that is there a real recovery taking place in China, he asked Prof. Yao what results we could be expected in the coming months in terms of economic growth.

Prof. Yao Yang addressed the question by mentioning the sharp decline in GDP in Q1 of 2020 (contracted by 6.8 per cent), and then elaborated on the current GDP, which has a negative growth of -4 per cent. He also expressed that to maintain a positive growth rate for the whole year government has initiated a stimulus package scheme worth 2 trillion RMB, which will be mostly spent on reviving consumption and employment development. Noting about investments which also have a negative growth of -10 per cent (year on year), he said that they could not rely on investments to bring positive growth rate in the economy.

Amb. Shyam Saran raised a question that even though the Chinese government has provided stimulus packages to revive the consumption, it is still not showing the kind of results that should be visible. Also, coming to the investment reviving part, he questioned that for some years, analysis shows that the Chinese economy has risen, and the growth is coming out of domestic consumption, not because of infrastructure investments and asked about Professor Yao Yang's opinion on the same.

Prof. Yao Yang agreed with Amb. Shyam Saran and stated that domestic consumption plays a vital role in reviving the economy much more than infrastructure investments do. In his opinion, the Chinese government should gear up with subsidy programs.

Amb. Shyam Saran phrased his next question to Prof. Chen Zhiwu. While pointing that the relations between China and the United States have soured and does not seem to be good at the moment, and at this point of time, he asked what results could be expected out of the meeting in Hawaii between China's State Councillor Yang Jiechi and US Secretary of State Mike Pompeo.

On this question, Prof. Chen expressed that we should not expect too much from the meeting in Hawaii because the fundamental drivers that have led to the worsening relations between the two countries have not changed at all. He said that the decoupling between the US and China is going to take a long time and not going to happen overnight.

Amb. Saran continued the conversation with Prof. Chen and asked him about the decoupling that was taking place between China and other nations. How is the Chinese leadership taking this decoupling and are they confident about this disengagement?

In response, Prof. Chen stated that the Chinese leaders in Beijing are confident that China can afford to face this decoupling in the long term. They have been preparing on the technology side to decouple Chinese tech sectors from US, and on the financial side, they are confident that they can decouple from the US. However, he warns that in the long run, there would be a lot of turmoil. He stated that once the Covid-19 situation stabilizes in the US, the E.U., and other countries, they will probably spend more time implementing decoupling. He also expressed that the impact of decoupling on the Chinese economy is more likely to show off in the year 2021 and 2022, particularly in the sectors of technology, financial services, and international trade.

Responding to the question concerning the direction Chinese economy is taking, Prof. Yao pointed, that recently, there is some disagreement at the leadership level regarding the measures taken in terms of recovery of the economy. He cited the example of the recent debate that ensued after the speech delivered by the Chinese Premier Li Keqiang, where he mentioned that the small economy, particularly, food stores, small shops, establishments had the potential of generating quite a large amount of employment, especially at a time when the economy has been rather severely affected as a result of the pandemic.

On the question of the employment situation in China and its importance for maintaining social stability - a central objective for the leadership, Prof. Yao explained that the Chinese Premier spoke about street employment, which started from Chengdu, the capital of Sichuan province, to temporarily increase jobs in the city and that had a significant impact on boosting employment. He stated that the Premier recommended the idea of street employment to other cities as well. But some of the first-tier cities expressed some reservation for this proposal because they believed that they do not need street employment. He addressed the question regarding the social stability of society in China by remarking that due to Covid-19, the social stability status has been affected. Going further, to achieve the goal this year, China has to achieve 5.6 per cent of growth. Therefore, the government of China will lean on fiscal stimulus to spur investment and consumption, which could push the 2020 budget deficit to a record high.

To Amb. Saran's question regarding the alteration happening with the Belt and Road Initiative (BRI) post-Covid-19 era, Prof. Chen stated that in his perspective, definitely, Covid-19 has dampened a lot of the excitement and focus on BRI, so one way to understand this is that BRI is going to sustain and stay essential for as long as the Chinese economy has no problems internally. He further added that in case the financial system and the economy face any crisis, then the BRI will be on the second priority list. The BRI project is directly linked to the current leadership, Xi Jinping and that “he will do whatever he can to keep the project alive as long as their domestic economy and society are not falling apart”.

On the question regarding China introducing crypto currency/ digital Yuan and the launch of an Asian currency with joint efforts of Japan, South Korea, Hong Kong and China, Prof. Chen was not sanguine about its success and observed that we should not imagine that digital Renminbi (RMB) will be more globally accepted than the actual physical RMB. In his opinion, the chances for the digital RMB to internationalize is way less as the latter is still not internationalized. On the Asian currency launch, Prof. Chen stated that if South Korea, Japan, and China can work together, it would be a big success and will be a start a new era of digital currency if these countries work together.

In response to Amb. Saran's question on whether he agrees to the fact that the role of Hong Kong as a financial Centre will continue to be very important for China or is it likely that that role will be diminished, Prof. Chen pointed that most people in Beijing fully appreciate how vital Hong Kong has been since the last four years, in terms of fast economic growth and internationalization of the Chinese economy and society. He stated his point that if the United States removes Hong Kong's 'Special Trade Status,' as they have already announced it some days back it might not have good impact overall. The roles played by Hong Kong as a key financial centre and buffer will diminish and it will no longer be served as an intermediary financial hub and a critical gateway between China and the world.

The session ended with a Q&A with the participants. On the question on how the Covid-19 situation could affect the utilization of foreign currency holdings of China, and is it a concern for the United States capital markets, Prof. Chen stated that at this point, there is more concern about whether the US government will seize the assets; there is less worry about the US restricting the Chinese capital to go into the US treasury market. But it is a concern for the managers of the foreign exchange reserves that how are they going to manage because the US capital market is the biggest market. No matter how far the political tensions will go between the two governments, still the foreign exchange reserves are piled with more and more US treasuries. Responding to a query on consumption shortages around the world and how this external component is going to impact the base of recovery in China, Prof. Yao noted that as far as export is concerned, China's export has grown by 1.4 per cent in April which is definitely due to the medical supplies demand and going further, he stated that China does not rely much on exports anymore.

*Report prepared by **Priyanka Madia**, Research Intern at Institute of Chinese Studies, Delhi.*

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