

Has the Chinese Economy Really Recovered? The Signs are Mixed.

By [Washington's Blog](#)

Global Research, June 06, 2009

[Washington's Blog](#) 6 June 2009

Region: [Asia](#)

Theme: [Global Economy](#)

There has been a lot of bullish news about China recently. Has the Chinese economy really recovered, or is there more to the story?

Bloomberg ran a fairly balanced take on China on June 1. After reviewing all of the bullish indicators, Bloomberg [noted](#):

China's banking sector is facing "grim credit and market risk" as corporate earnings fall because of an over- concentration of lending in certain industries and regions, the China Banking Regulatory Commission said today in its 2008 annual report.

Real estate is among industries that may default on loans, causing growing pressure on Chinese banks after economic growth dropped to the weakest in almost a decade, the statement said.

Similarly, Michael Panzner, after noting many positive signs, [writes](#):

Is the China recovery story all it's cracked up to be? Evidence suggests that might not be the case, and that the economic outlook remains less-than-upbeat, to say the least.

Ironically, another report published on Monday by the China Banking Regulatory Commission offers one reason for pessimism. According to the CBRC ([via Dow Jones](#)), "the country's economy faces growing downward pressure as the global financial crisis has yet to run its course." The regulator added that "the banking industry faces 'serious' credit and market risks as the domestic economy encounters its 'most difficult year in the new century.'"

That's not all. In a statement released today, a Chinese government official noted signs of trouble in a key sector. Vice Minister of Commerce Zhong Shan warned "exporters were facing 'unprecedented difficulties' at present and that the situation would not improve amid the global economic downturn," [Reuters reported](#). "It is increasingly difficult for us to make a quick turnaround, and the trade situation will not be optimistic in the second half of this year," Zhong said in a statement on the ministry's website."

At least one closely watched data series also casts doubt on the notion that an economic revival is at hand. Last week, [Reuters wrote](#) that "the decline in China's power output accelerated in the first 10 days of May to 3.9 percent from a year earlier, the influential *Caijing Magazine* reported on Monday, providing the latest evidence that the Chinese economic recovery still lacks a solid footing."

In addition, “nationwide electricity consumption via major grids had fallen 4.3 percent in the first 10 days of May, also 0.7 percentage points sharper than that for the last 10 days of April, it said, confirming earlier local media reports. The power data is considered by some as more of a leading indicator than manufacturing and export data.”...

According to the [London Evening Standard](#), a leading energy analyst found strong evidence that the run-up in oil prices in recent weeks stemmed from stockpiling, or hoarding, by the Chinese. Neil McMahon of Bernstein Research concluded that the rise “reflects not strengthening demand, but rather China’s efforts to boost its strategic petroleum reserve.”

Even businesses with potentially more of a direct stake in China’s domestic economy are questioning the Asian nation’s near term prospects. Citing [the latest issue of Woman’s Wear Daily](#), Bloomberg reported that U.K. luxury retailer Harvey Nichols plc is “staying away from mainland China as most consumers don’t earn enough to buy its fashions and real estate prices in big cities are too high.”

In sum, while the nation’s growth strategy and comparative advantages may eventually prove the optimists correct, right now, at least, the China recovery story seems to have lots of holes in it.

China expert Michael Pettis [analyzes](#) a Financial Times [article](#) written by Wang Qishan – a Vice premier in the State Council and “presumably one of the top three or four economic policy decision-makers in China”:

It starts out, correctly I think, by warning that the global crisis is far from over. “The global financial crisis is still spreading,” Wang warns, “The world economy is going to get worse before it gets better, and the situation remains serious.” ... China is the country that most desperately needs foreign demand to absorb its excess capacity. In a world of contracting demand, China is the country that is most likely to suffer from protection, for the same reason that it is the country that benefits most from absorbing other country’s badly-needed demand. In that case it is not enough to say that China is just doing what everyone else is doing (and never mind that it is much harder for foreigners to invest in China or sell to China than it is for China to do either abroad), since any dispute that resolves itself in greater trade protection hurts China worse than it hurts the other disputant...

Pettis then goes on to respond to the statement by Chen Deming, head of China’s Ministry of Commerce, that Chinese exports need to remain the main engine in the Chinese economy:

I think in one sense Minister Chen is right – foreign demand is still the engine of Chinese growth – which is one of the reasons I am so [pessimistic](#) about medium-term growth . . . The fact that the editorial and the original article from which it was drawn were both published, and seem to be arguing a case, gives some indication, I think, of the ferocity of the debate taking place about the nature of the stimulus package. One side says: Before we can fix the economy we need relief, and that is most likely to happen by reinforcing the existing economic structure. The other side says: The longer we take to postpone the adjustment, the worse. For the other side of the debate, Hu Shuli in last week’s *Caijing* [insists](#) that “Beneath the surface of China’s ‘warming’ economy are structural impediments to long-term growth that demand attention – now.” She dismisses the recent optimism about China’s “bounce”

back with “The ‘warming’ is more show than substance.” and she goes on to say:

Since we know that credit expansion is not the best economic healer, we should spend the coming days thinking about long-term approaches that will help China survive the crisis and pursue lasting development.

China is being forced to rebalance. It’s clear that, regardless of the angle from which we examine the situation, our economy is being squeezed by internal and external crises. Excessive consumption in the United States is a root cause of the global financial crisis. Instead of complaining about this fact, or even quietly congratulating ourselves, China must consider what to do if the United States learns its lesson and, for example, gradually raises its household savings rate. If external demand for Chinese goods is declining, how can internal demand rise?

At this juncture, structural adjustment should not be empty talk. It must involve a series of basic policies that deepen the nation’s economic reform. Structural adjustments can only follow the market’s lead and, for the most part, involve breaking up monopolies, opening the market wider, relaxing controls, and getting the pricing mechanisms right.

Instead of betting even more heavily on foreign demand to bail China out, in other words, China must urgently move towards policies that force the transition, even if those policies are painful in the short term. And it is not just Caijing that is voicing criticism about the current stimulus policies. A number of very prominent Chinese economists have been scathing (at least in private, so I cannot reveal their names) about the failure to have taken the appropriate steps when conditions were optimal, and are now insisting that to continue increasing reliance on foreign demand is going to create huge problems for China. Increasingly I am hearing people here say that, although few expect a “collapse”, whatever that means, China is facing its own “lost decade” of sub-par economic growth and a very difficult transition. As regular readers know, I am very inclined to agree.

Finally, Brad Setzer [weighs in](#) on China’s dollar trap:

China currently has a bit over [\\$1.5 trillion in dollar assets](#), as not all of its \$2 trillion in reserves (and more like \$2.3 trillion to \$2.4 trillion in government assets abroad) are in dollars. About ½ of the total is result of China’s purchases in just two years, 2007 and 2008. China’s trade surplus isn’t shrinking, at least not in dollar terms. [Lex’s argument](#) that China’s surplus is waning can be challenged.* And even if China’s trade surplus stabilizes in dollar terms and shrinks relative to China’s GDP, China is on track to double its foreign assets – and its US holdings – over the next four years. Think a \$350-400 billion annual increase in China’s dollar assets, and a \$500b plus increase in China’s foreign assets.

That prospect should scare China’s leaders...

To be clear, the basic risk China is running hasn’t changed all that much recently. China’s government fundamentally is overpaying for dollars (and euros) to hold the RMB down to help China’s exporters. That policy always has carried with it a high risk of future financial losses.

The current crisis hasn’t fundamentally changed that basic reality...

The basic message in [Geithner’s Beijing speech](#) was clear: the goal of both US and Chinese policy should be to move away from the current unbalanced

relationship.

Our common challenge is to recognize that a more balanced and sustainable global recovery will require changes in the composition of growth in our two economies. Because of this, our policies have to be directed at very different outcomes.

In the United States, saving rates will have to increase, and the purchases of U.S. consumers cannot be as dominant a driver of growth as they have been in the past. In China growth that is sustainable growth will require a very substantial shift from external to domestic demand, from an investment and export intensive driven growth, to growth led by consumption. Strengthening domestic demand will also strengthen China's ability to weather fluctuations in global supply and demand.

If we are successful on these respective paths, public and private saving in the United States will increase as recovery strengthens, and as this happens, our current account deficit will come down. And in China, domestic demand will rise at a faster rate than overall GDP, led by a gradual shift to higher rates of consumption. Globally, recovery will have come more from a shift by high saving economies to stronger domestic demand and less from the American consumer.

Seems like a vote for change, not more of the same...

Until now, China's policy has been dominated by concerns about the impact of any change in China's exchange rate on China's exports. Yet it is hard to see how China can realistically scale back even the pace of increase in its dollar exposure so long as it is running a large trade surplus and pegging to the dollar.

Chinese policy makers have been searching for a way to avoid adding to their dollar exposure without changing their dollar peg ... China's efforts won't get China very far so long as China's capital account is closed and China pegs to the dollar. As China comes to the same realization, the pressure on it to adjust its policies will grow...

Change isn't without its risks. One of the key factor pushing China to adjust - its concerns about the safety of its US portfolio (or, in my view, its China's belated recognition that holding its exchange rate down has costs as well as benefits, as it requires continuously overpaying for dollar and euro denominated bonds) - also makes the market nervous. And a nervous bond market tends to make policy makers a bit nervous.

On the other hand, if China (and the US) double down, the underlying problem would in some sense only get worse. The basic issues won't change. But the stakes will be even higher.

The sources of pressure for change are increasingly obvious. Even in China. That's good. But transitions aren't easy. Deficits - even shrinking deficits - have to be financed. And financing an orderly (think gradual) adjustment poses particular challenges. For everyone.

So are the signs on balance good or bad for China?

There are, indeed, some positive signs. But everything is not as rosy as the news headlines would suggest.

The original source of this article is [Washington's Blog](#)
Copyright © [Washington's Blog](#), [Washington's Blog](#), 2009

[Comment on Global Research Articles on our Facebook page](#)

[Become a Member of Global Research](#)

Articles by: [Washington's Blog](#)

Disclaimer: The contents of this article are of sole responsibility of the author(s). The Centre for Research on Globalization will not be responsible for any inaccurate or incorrect statement in this article. The Centre of Research on Globalization grants permission to cross-post Global Research articles on community internet sites as long the source and copyright are acknowledged together with a hyperlink to the original Global Research article. For publication of Global Research articles in print or other forms including commercial internet sites, contact: publications@globalresearch.ca

www.globalresearch.ca contains copyrighted material the use of which has not always been specifically authorized by the copyright owner. We are making such material available to our readers under the provisions of "fair use" in an effort to advance a better understanding of political, economic and social issues. The material on this site is distributed without profit to those who have expressed a prior interest in receiving it for research and educational purposes. If you wish to use copyrighted material for purposes other than "fair use" you must request permission from the copyright owner.

For media inquiries: publications@globalresearch.ca