

Landing Without Cables: Assessing China's Near-Term Economic Prospects



Deepak Bhattasali

World Bank

US-China Business Council, Forecast 2009

January 29, 2009



Prologue

- ◆ Are Chinese statistics reliable?
- ◆ Are Chinese macro-management tools adequate?
- ◆ Where was the Chinese economy headed before 2008?
- ◆ What are the concerns for 2009?



Chinese Statistics

- ◆ Lots of progress, but incomplete coverage and quality control still problems
- ◆ Large revisions common
- ◆ Cross checks needed—seasonal adjustment, partner country data, proxies
- ◆ Perversely, much more reliable during abnormal times than normal



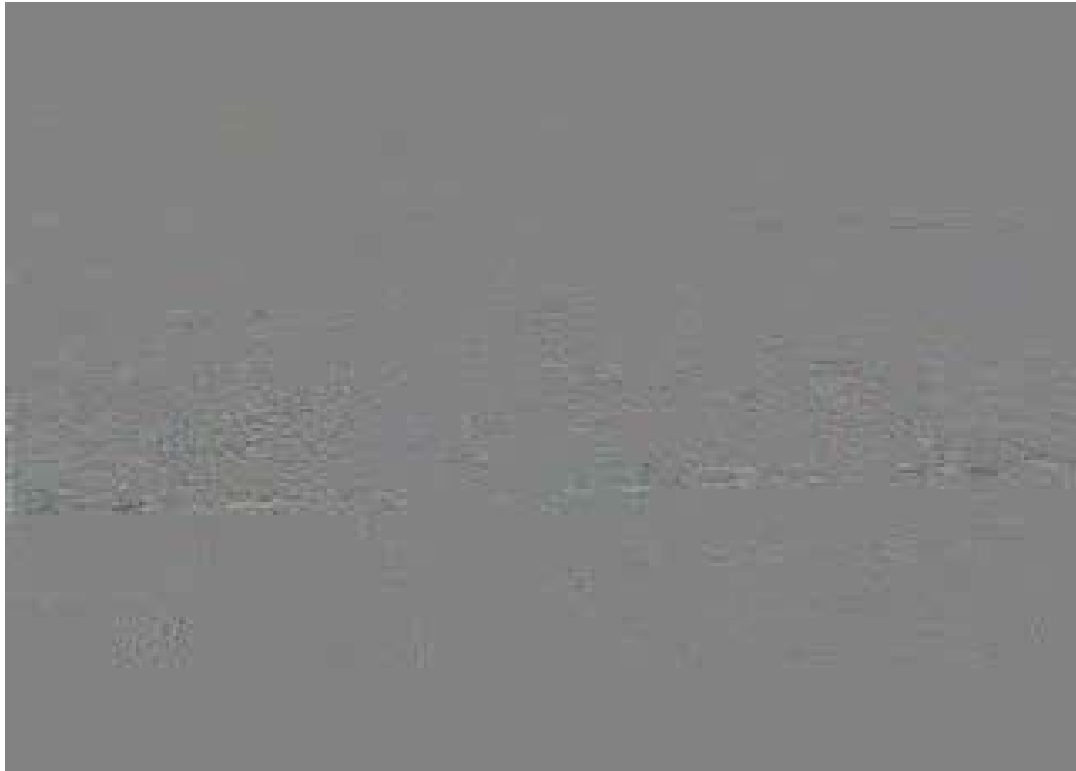
Macro-management Tools

- ◆ Transiting between command and market
- ◆ Monetary policy—weak transmission
- ◆ Fiscal policy—sub-national and off-budget transactions
- ◆ Exchange rate—relatively stronger
- ◆ Administrative guidance--strongest



Landing a Plane on a Carrier is Never Easy, On a Pitching Sea it is Extremely Difficult and Hazardous

Normal
Landing

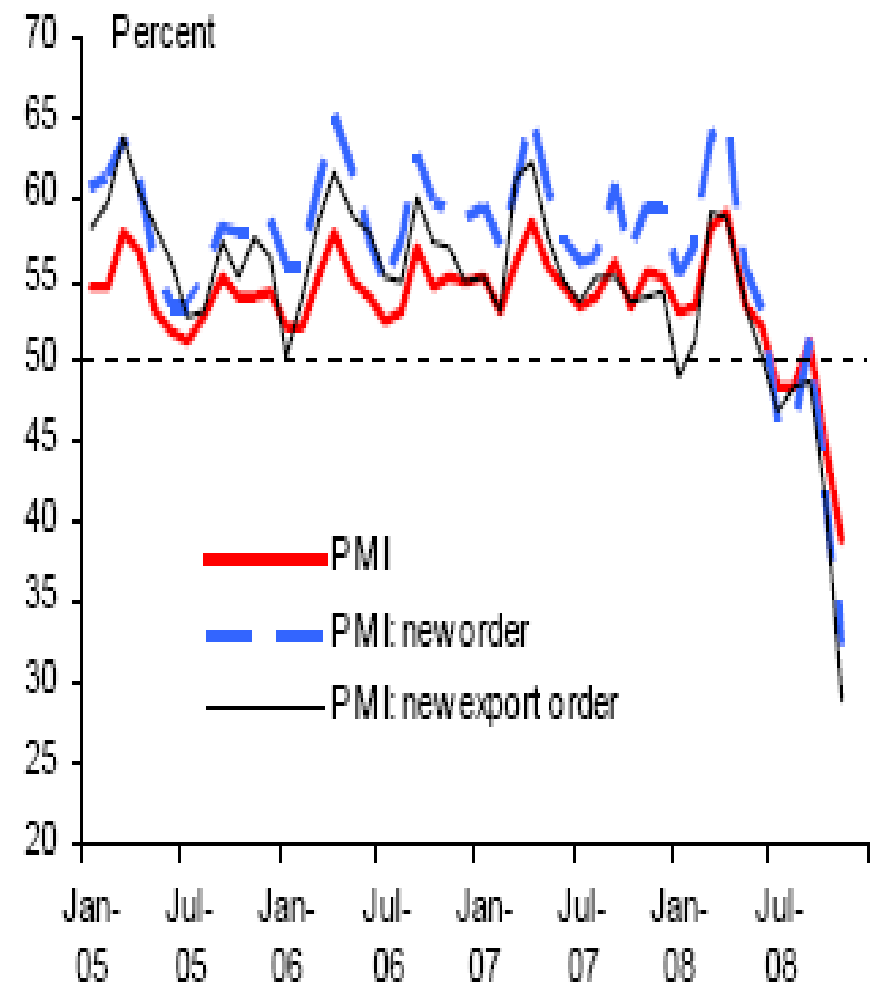
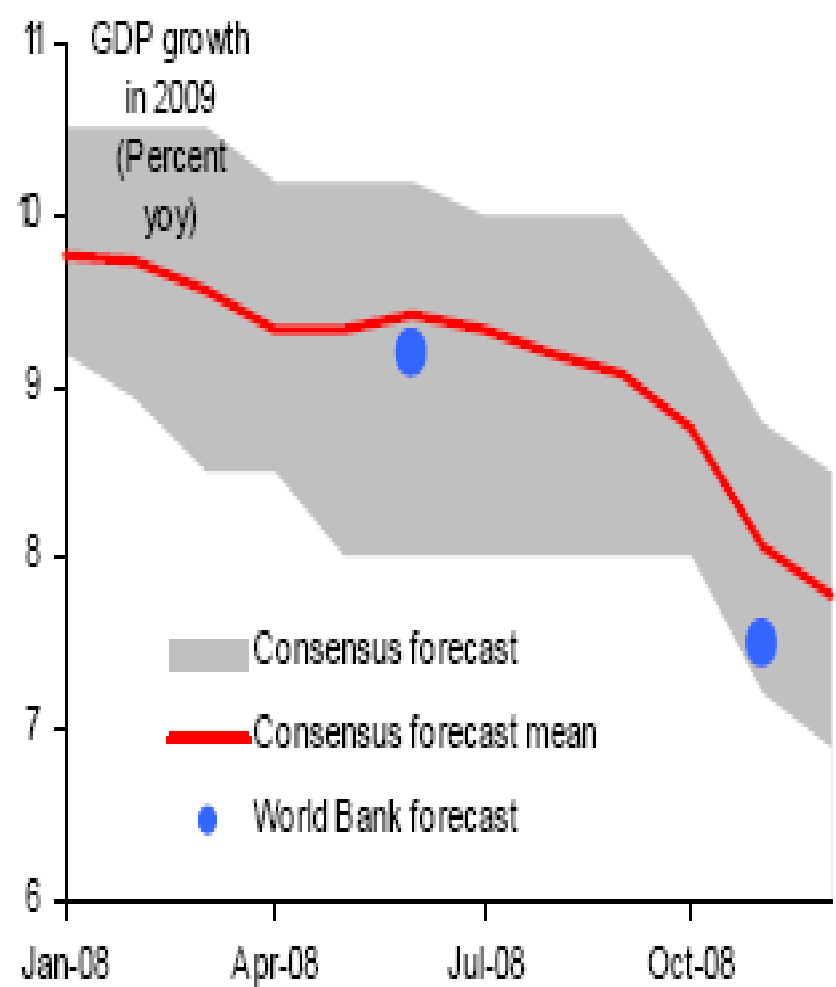




Economic Developments in 2008

A. Forecast of 2009 GDP growth has been downgraded continuously in 2008

C. PMI at new record low suggests the worst is yet to come

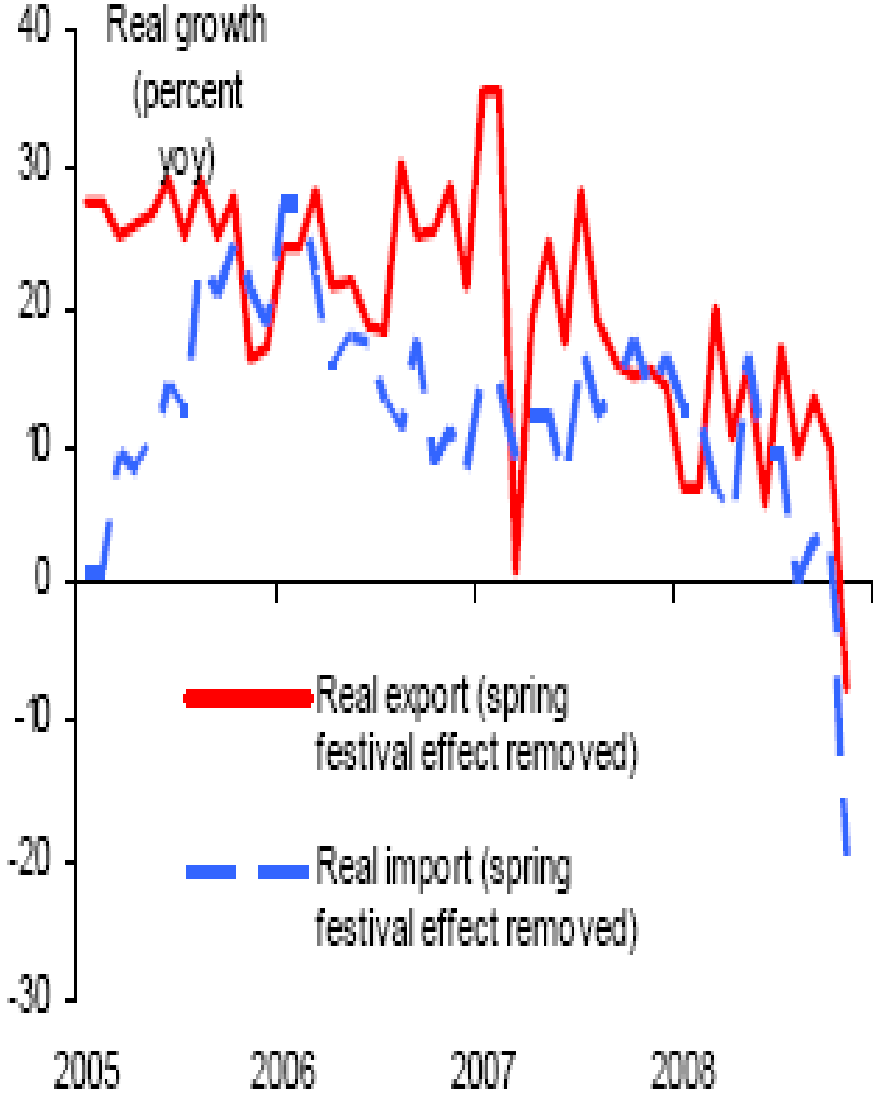
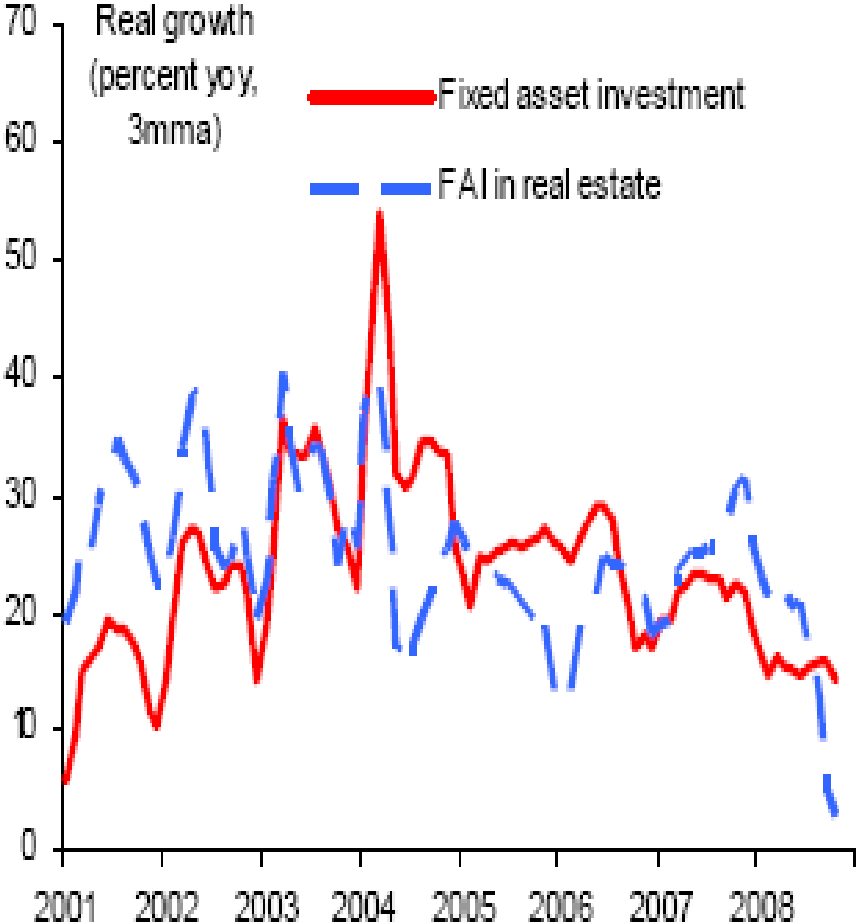




Economic Developments in 2008

Real exports have fallen

Figure 5. Investment growth is down on 2007

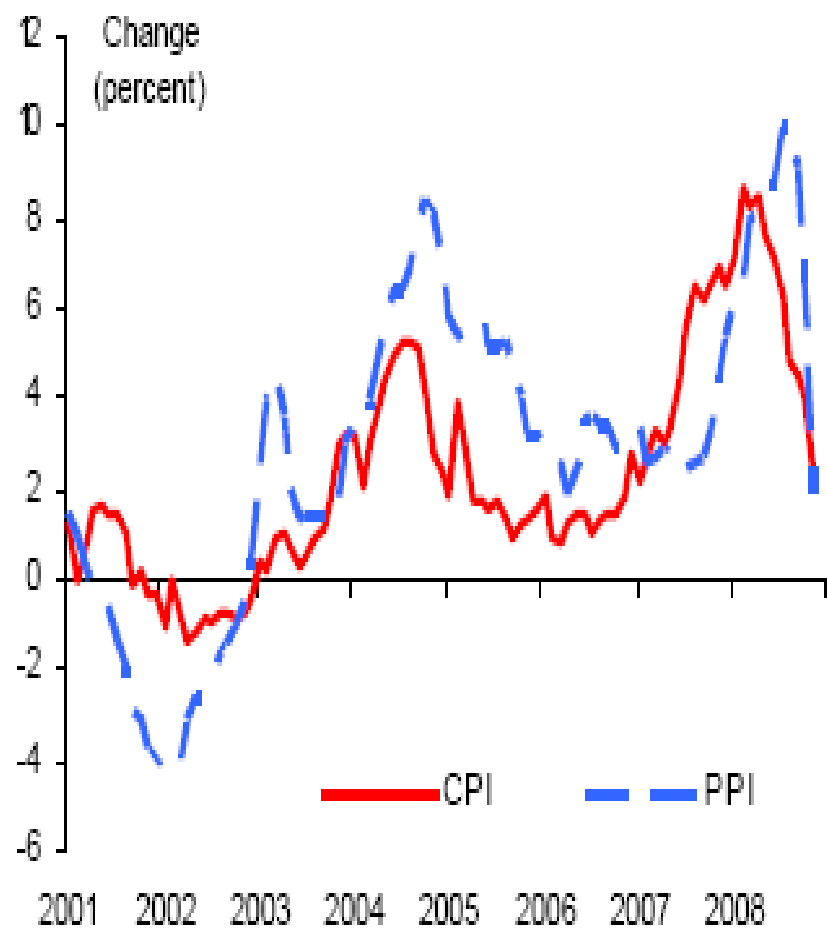
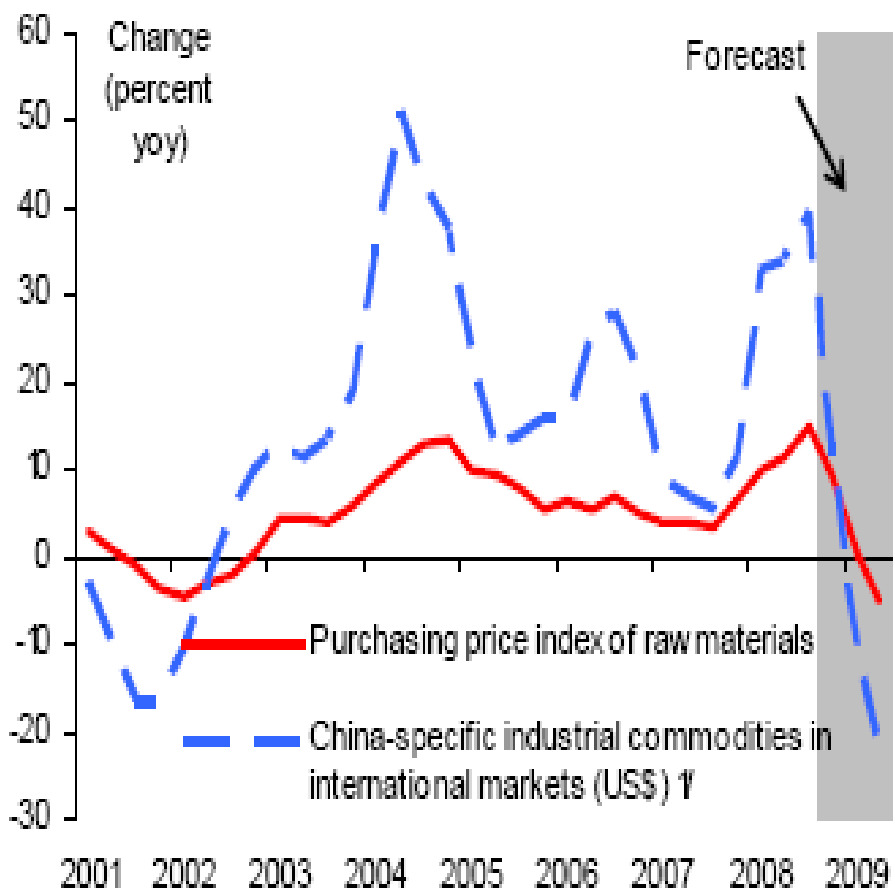




Economic Developments in 2008

Figure 12. Sharply lower commodity prices drive down raw material price inflation

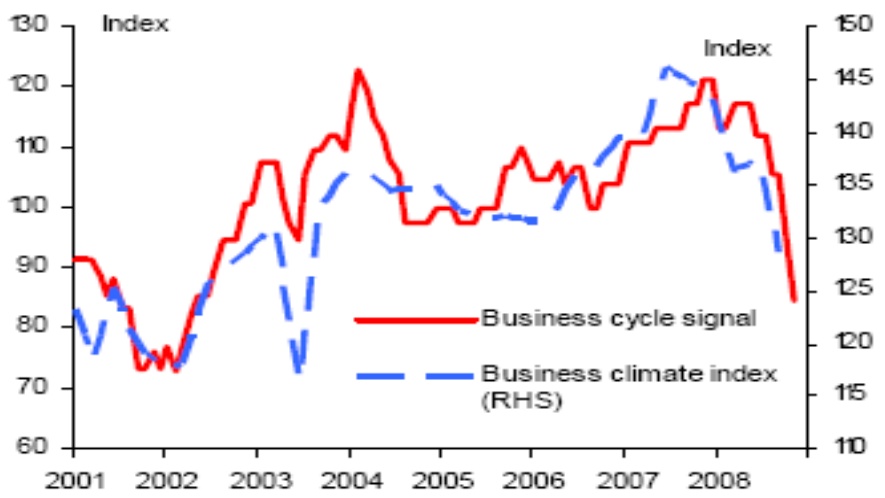
D. Inflation rate has come down quickly





Economic Developments in 2008

Figure 5. Coincident indicators



Source: CEIC, World Bank staff estimates.

Figure 6. Leading indicators



Source: CEIC, World Bank staff estimates.

Figure 7. Purchasing managers' index (PMI) of the manufacturing industry

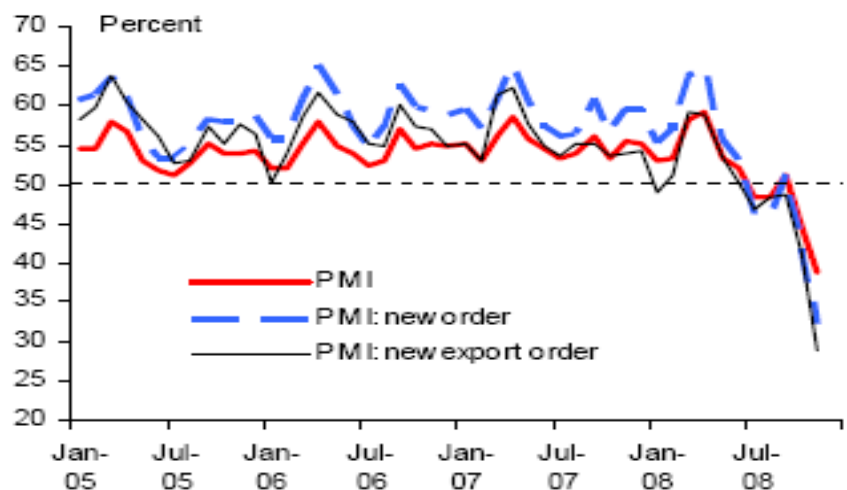


Figure 8. Consumer confidence and expectation





Economic Developments in 2008

Figure 53. Real trade growth



Figure 58. Export real growth by sector (II)

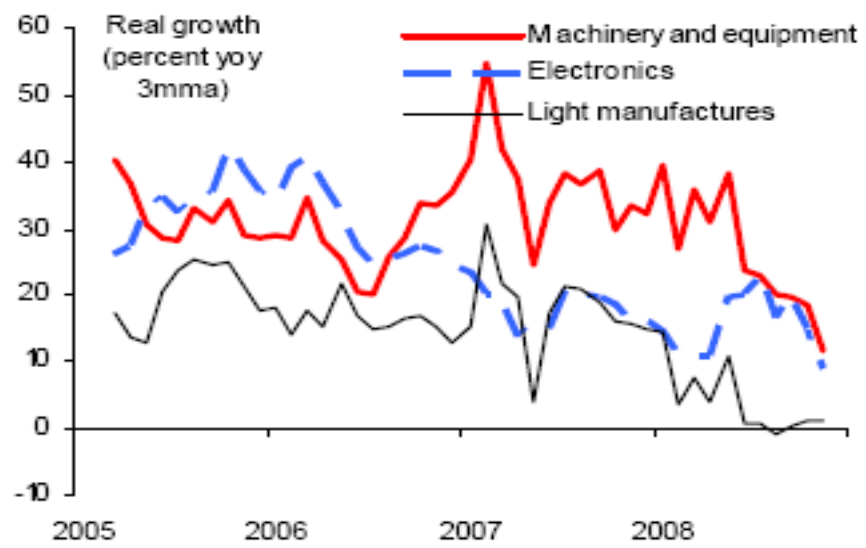


Figure 59. Import real growth by sector (I)

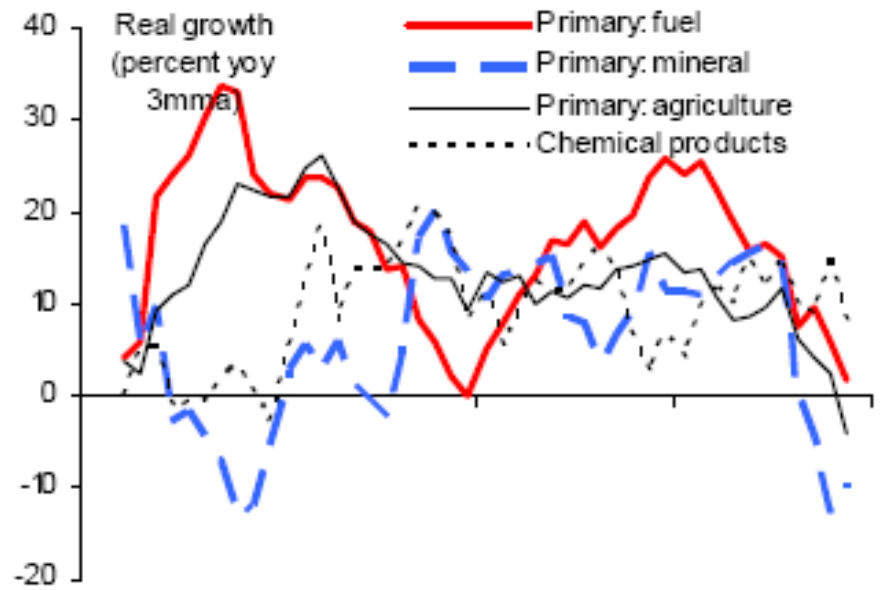


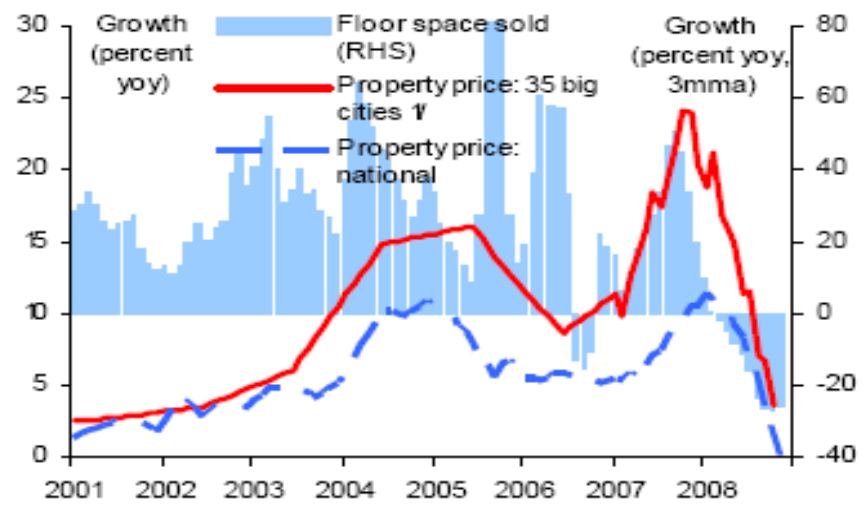
Figure 67. PE ratio





Economic Developments in 2008

Figure 21. Property sales and price



Source: CEIC, World Bank staff estimates.
1/ The biggest 35 cities in China.

Figure 23. Property construction

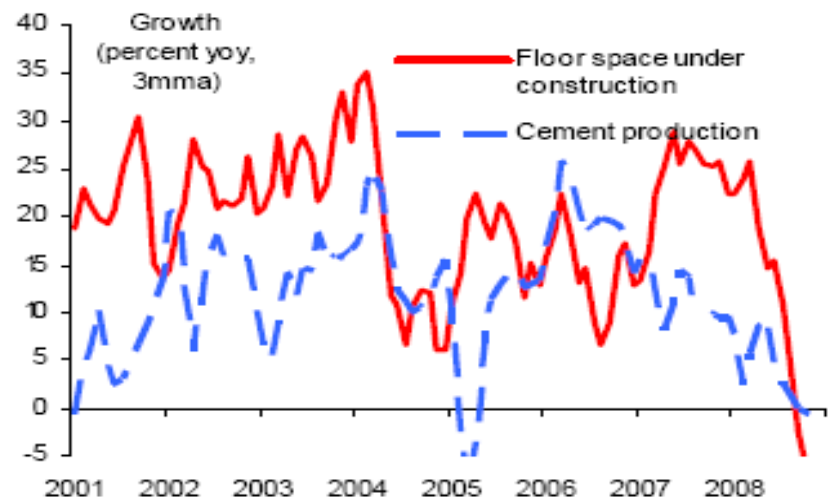


Figure 25. Retail sales of consumer goods



Figure 26. Retail sales of large retailers





Economic Developments in 2008

Figure 31. Urban income and expenditure

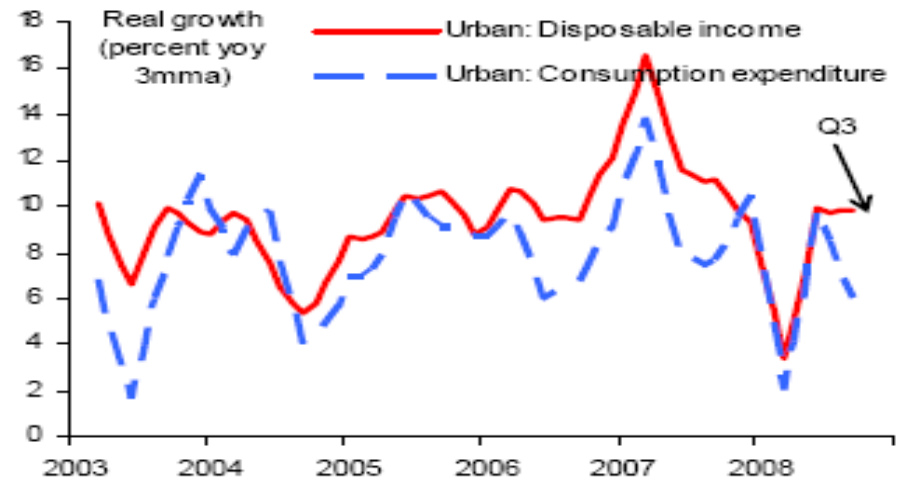


Figure 32. Rural income and expenditure

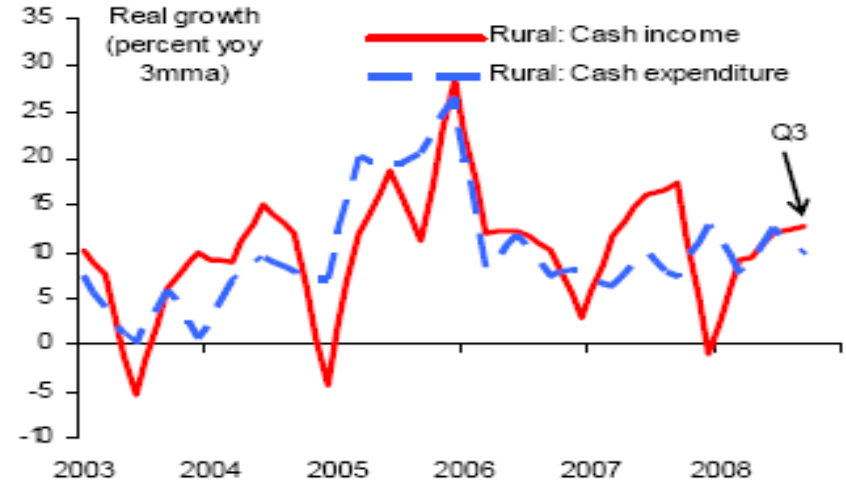


Figure 38. Loan and deposit growth

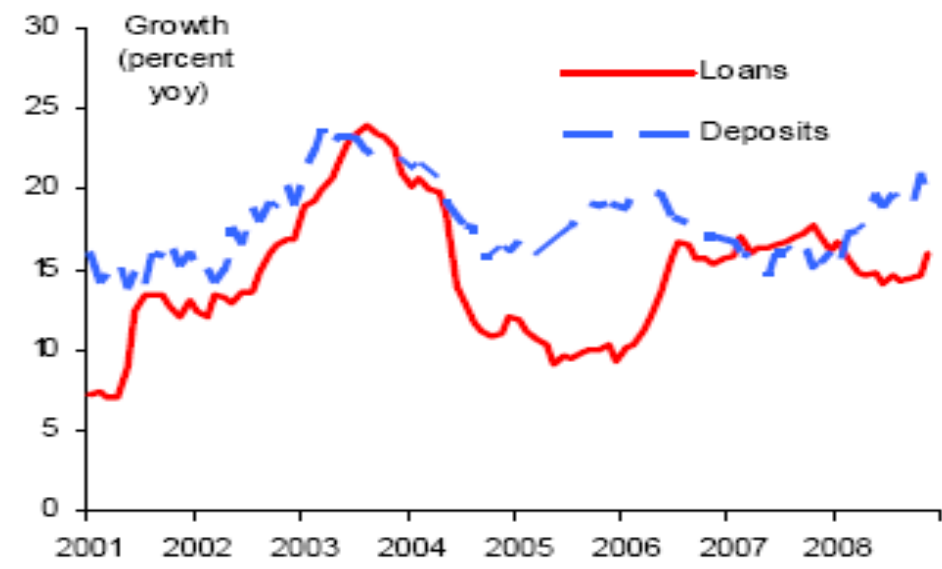
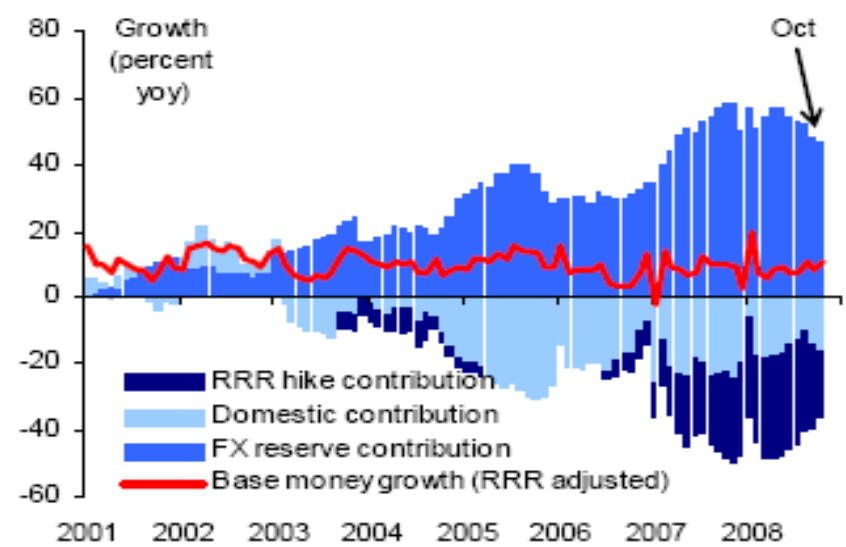


Figure 43. Breakdown of base money growth





Projections for 2009: The Context

- ◆ **One** central concern

- Employment

- ◆ **Two** types of rebalancing

- External to domestic demand

- Investment to consumption

- ◆ **Three** macro-management challenges

- Fiscal space and monetary expansion

- Government spending, leads and lags

- Contingent liabilities and complementary finance



Employment

- ◆ Urban employment creation is key
- ◆ Meaningless magic numbers
 - Net addition to labor force
 - Pattern of economic activity
- ◆ Employment and social distress
- ◆ Things to watch
 - Construction
 - Internal migration
 - Social spending initiatives



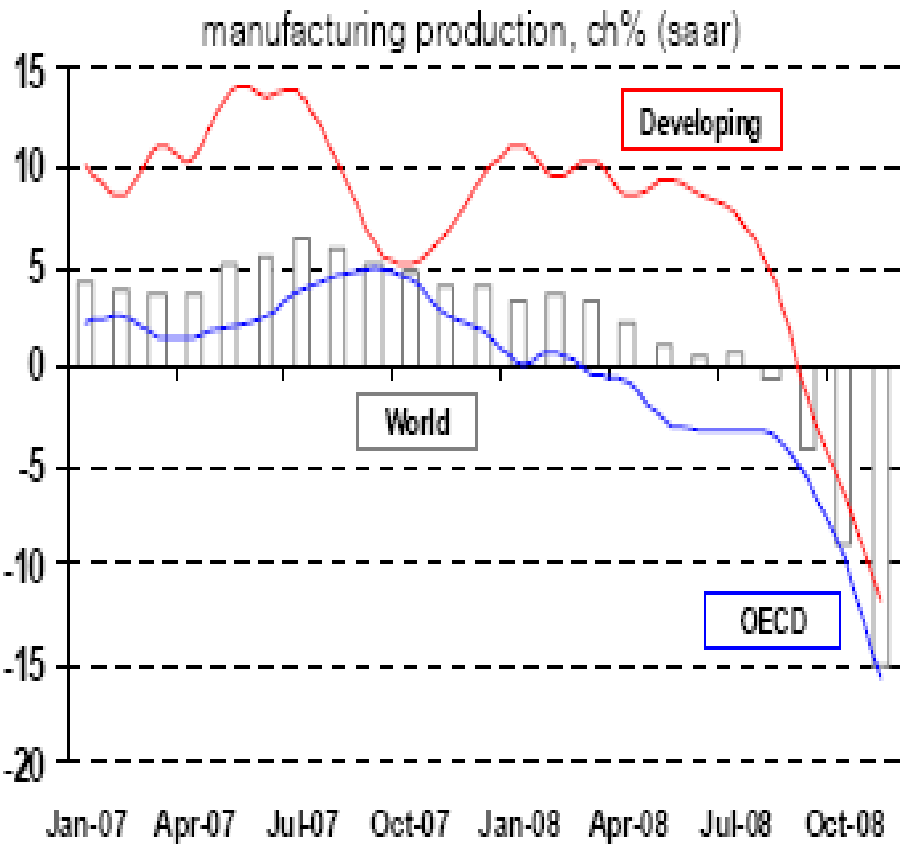
Rebalancing 1

- ◆ Everyone expects a very poor global trade environment, so net export contribution is likely to be zero, or near to it, despite decline in imports
- ◆ But China has surprised in past downturns, and incentives to export are still strong
 - Capacity
 - VAT rebates

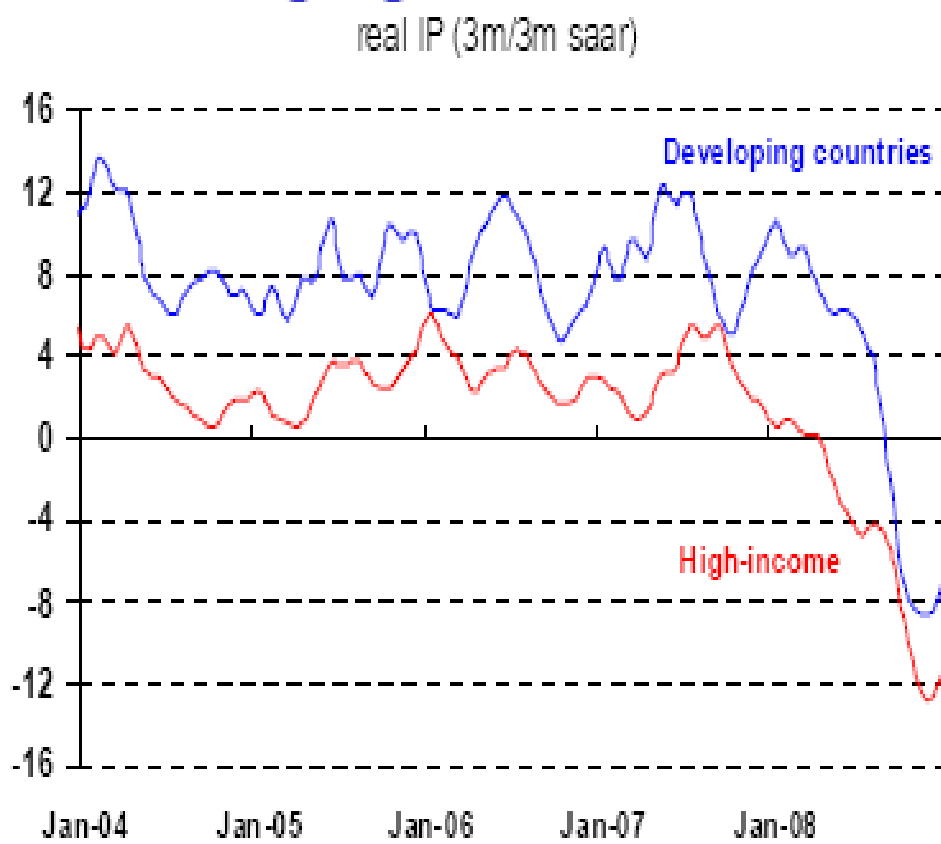


Rebalancing 1

Global industrial production plummets into 4th quarter of 2008...



Developing countries' IP plunges, mirroring high-income countries



Rebalancing 1

Global Indicators

(Percentage change per annum, unless otherwise specified)

	2006	2007	2008e	2009f
GDP volume: World	4.0	3.7	2.5	0.9
<i>Memo item: World GDP at PPP weights</i>	5.0	4.9	3.6	1.9
High-income countries	2.9	2.4	1.3	-0.1
Developing countries	8.8	9.7	6.3	4.5
Industrial production: World	4.5	4.4	3.0	...
High-income countries	2.9	2.4	0.7	...
Developing countries	8.8	9.7	8.5	...
Export volume (GNFS): World	9.8	7.5	6.2	-2.1
High-income countries	8.6	6.2	5.9	-3.7
Developing countries	13.2	10.8	7.0	2.1
Trade Prices (\$): Manufacturing (MUV)	1.6	5.5	9.0	2.1
Oil (\$/bbl)	64.3	71.1	97.0	47.8
Non-oil commodities	29.1	17.0	22.4	-23.2
Nominal interest rates:				
SLIBOR (percent p.a.)	5.2	5.3	3.3	1.9
LIBOR (percent p.a.)	3.1	4.3	4.9	3.8
Financial flows				
FDI (\$billion)	365	532	480	
Gross Capital flows ^a (\$billion)	494	652	371	377
Equity placement (\$bn)	111	194	47	54
Bond financing (\$bn)	137	146	69	73
Lending (\$bn)	246	312	254	232

Source: DECPG, January 2009. Estimates and projections based on GEP-2009, released 12-9-2008.

Note(s): a. Gross inflows 2008 are preliminary. Figures in **bold** represent changes this month.



Rebalancing 1

Global Outlook for China: Comparison with Previous Downturns
(Constant Prices, Average Yearly Changes)

	<u>1997</u>	<u>1998</u>	<u>2000</u>	<u>2001</u>	<u>2007</u>	<u>2008(e)</u>	<u>2009(p)</u>
World GDP	3.8	2.5	4.2	1.7	3.7	2.5	0.9
China-Weighted World GDP <u>a/</u>	3.7	1.7	4.3	1.4	4.1	2.9	1.1
World Imports	9.7	4.8	12.2	0.3	7.4	6.2	-2.1
China							
Exports	22.6	7.1	30.6	9.6	15.3	10.9	3.5
GDP	9.3	7.8	8.4	8.3	11.9	9.0	7.5



Rebalancing 2

Figure 14. China's investment heavy, industry-led economy

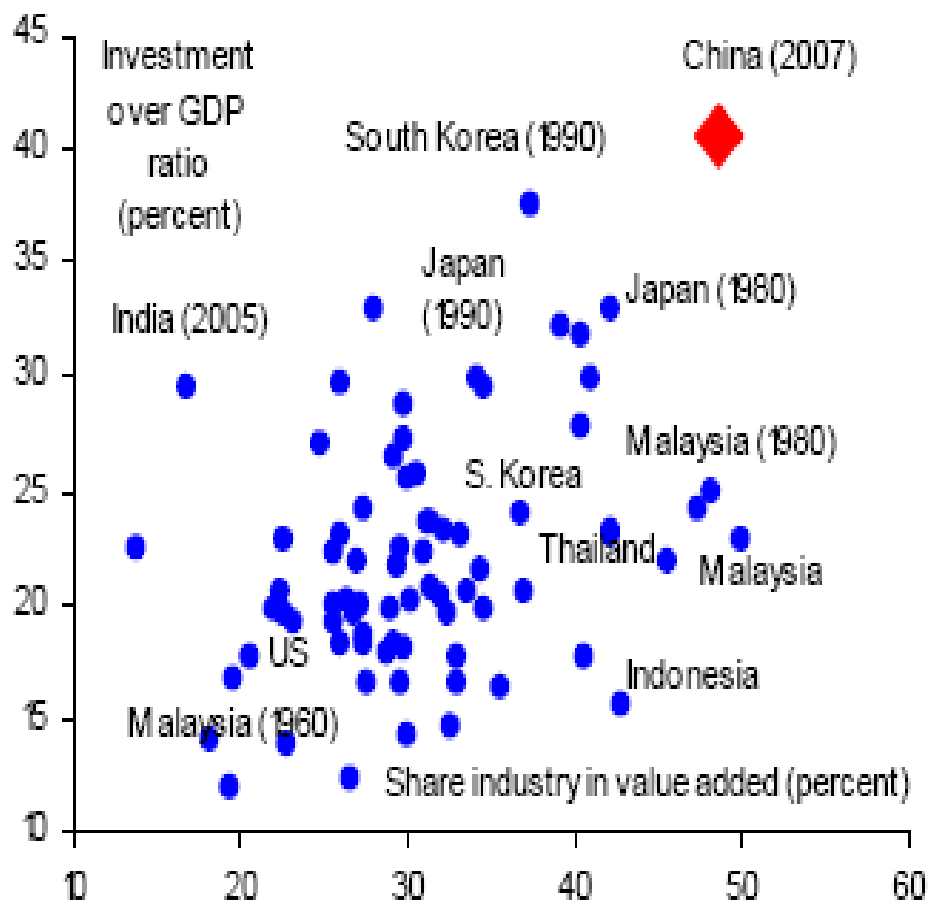
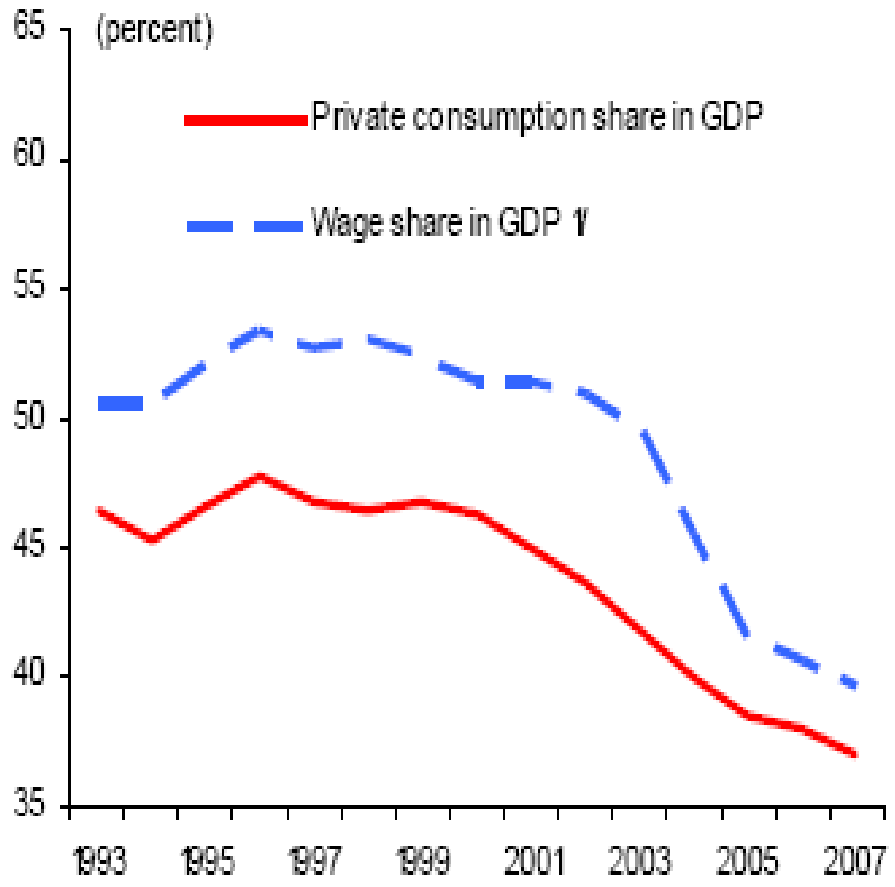


Figure 15. Structure of the economy is key to increasing the role of consumption



A cluster of several dice in various colors (white, black, red) is positioned in the top-left corner of the slide. A thick red horizontal bar is located at the top of the slide, partially overlapping the dice.

Rebalancing 2

- ◆ Much depends, therefore, on fiscal stimulus and the timing of inflationary pressures
- ◆ With the November 9 plan, the government identified measures in 10 areas to boost domestic demand and growth in 2009 and 2010.
 - Public housing projects
 - Rural infrastructure investment
 - Transport infrastructure
 - Health and education
 - The environment
 - Innovation and restructuring
 - Post-earthquake reconstruction
 - Household income
 - Rolling out the VAT reform nationwide in 2009
 - Increasing bank lending



Macro-Management Challenges

Fiscal Space

Table 2. A tentative fiscal scenario (percent of GDP)

	2007	2008	2009
Budgetary revenue	20.6	21.2	20.5
Budgetary expenditure	20.0	21.6	23.1
Budgetary balance	0.6	-0.4	-2.6
General government balance 1/	2.0	0.9	-1.7
Fiscal impulse, based on			
Budgetary balance	-1.4	1.0	2.2
General government balance	-1.6	1.1	2.6

- ◆ There is fiscal space
- ◆ When will inflation rear its ugly head?



Macro-Management Challenges

Government Spending—Leads & Lags

- ◆ Direct boosts to consumption limited, so lead time longer
- ◆ Off-the-shelf investment projects exist because of 2006-2008 contraction
- ◆ Can ramp up new projects, but monitoring and supervision is challenging



Macro-Management Challenges

Fiscal Space, Yes, But For How Long?

- ◆ Length of global downturn and second bite at the apple
- ◆ How much can sub-national governments do?
- ◆ Contingent liabilities—local governments, SOE, financial institutions