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Lower but Stabilizing Growth

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Supply-Side Reform and Monetary Policies

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New Forces for Chinese Economic Growth

As China's economy steps into the "New Normal", the growth forces should shift into a stage characterized by advanced forms, a complex labor division and a rational structure.

Migrant Workers Becoming Citizens to Drive Economic Restructuring

The citizen-oriented development of migrant workers will increase their consumption in cities and stimulate economic growth.

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On the Development Models and Experience of SEZs in China

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The Shenzhen "Going East" Strategy Seminar
Nov. 18, 2015, Shenzhen

Seminar on Building a High-Level Think Tank
Dec. 10, 2015, Shenzhen

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The "13th Five-Year Plan" and Long-Term Chinese Economic Growth

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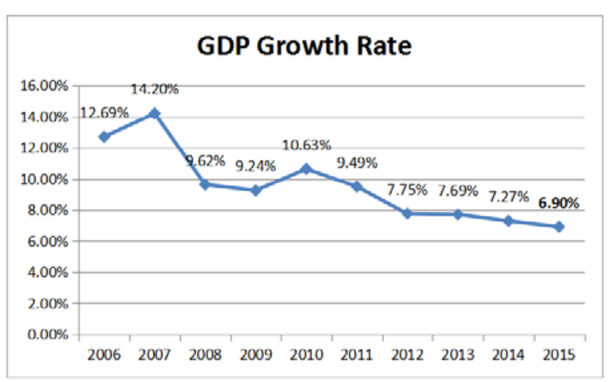

Source: National Bureau of Statistics

Industrial output was up 6.1% y/y in 2015, down 2.2 pps from 2014. But industrial output performed better in H2 than in H1, showing a sound trend within the year. Fixed asset investment rose 10% y/y in 2015, down 5.7 pps from 2014. But various indicators in Q4, such as new project openings, suggest investment will pick up in early 2016.

M1 and other key financial indicators show a loosening monetary policy with a continuous interest rate cuts in 2015. In the end of June, M1 rose only 4.3% y/y, still at a very low level. After July, M1 quickly rebounded and in the end of year, M1 growth rate rose to 15.7% y/y.

The IMF decided to add the yuan to the SDR basket in November. We expect more yuan internationalization consistent with Xi's "Belt and Road" initiative. Joining the SDR also signals more financial reforms to come, which will generate steadier economic growth. The inclusion of the yuan in the SDR may help the yuan stabilize, though the differential between onshore and offshore currency valuations has persisted recently.

Pollution in China has attracted much international attention. On December 19th, the notoriously polluted city of Beijing once again issued a level-four red alert, the most serious level in the four-tier warning system. China's pollution is a consequence of its rapid industrialization. *The "new normal" – a relatively slower growth rate for structural change -- is partly a response to the problem of heavy pollution.* Pollution is also pushing structural change, as industry must upgrade with environment-friendly products, by adopting successful BYD electric cars, for example.

The Central Bank on January 17th announced that it would raise the reserve requirement ratio for yuan deposits in offshore yuan-clearing banks, to stave off currency speculation. Meanwhile, China's foreign reserves shrank by a half trillion in 2015, to $3.33 trillion. We expect the Chinese government to use such capital controls, and its still-gigantic foreign reserves, to stabilize the yuan, and to weaken it against the dollar, until the full correction (from overvaluation) is complete. Capital controls are periodically necessary, to allow China to stabilize its markets, given the country's immature financial market, and the newness of its entry into the liberalized international capital markets.

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Supply-Side Structural Reform and the Orientation of Monetary Policies

Prof. FAN Gang

At present, supply-side structural reform in China is becoming increasingly important and urgent. Some believe it is imperative to make necessary adjustments through supply-side reform because the marginal effects of monetary and fiscal policies will decrease progressively.

Supply-side structural reform generally includes such popular issues as institutional reform, education development, innovation and industrial restructuring. These issues involve productivity improvement and long-term growth trends, e.g., the rise of the potential growth rate. Reform in this regard is often believed to be a long-term issue which cannot be solved once and for all in the short term. It is currently the most important issue in China, and it poses the greatest challenges.

Monetary policies and macro policies make short-term adjustments. When the supply is given, if a demand surplus suddenly occurs, it is often necessary to curb surplus to avoid inflation. When the demand falls short, it is imperative to make up for the shortage through macro policies.

Strictly speaking, macro policies adjust the demand side while reform polices adjust the supply side, and both of these policies are necessary. In different circumstances and at different time points, we need to use policies to stabilize demand-supply relations so as to facilitate the continuous growth of the Chinese economy. We must not replace short-term policies with long-term policies, or else the financial crisis cannot be addressed. To counter this crisis, we will have to adopt demand-side policies.

On December 1st, 2015, the IMF announced that the RMB would join the SDR on October 1st, 2016. This has been praised as a major milestone for the integration of the Chinese economy into the global financial system. Although the RMB still has a long way to go before becoming a genuine international reserve currency, this still marks the rise of China's power and stability of the Chinese currency.

To further reform the Chinese forex system, we should not resume the system of being pegged to the USD that China adopted in the past. Instead, the RMB should be related to the currencies of a variety of nations, thus encouraging more countries to use the RMB due to its reserve function and raising the international development of the RMB to a new level.

The RMB is very stable against the USD. However, the Japanese Yen and Euro have depreciated over the past few years. Furthermore, currencies in emerging economies such as the AUD and CAD have also depreciated considerably against the USD. As a result, the USD-pegged RMB has become seriously overvalued, forming expectations for RMB depreciation in the market.

The real weak point in China is direct financing. 2015 witnessed serious fluctuations in the Chinese capital market. People are calling for the stock market to be improved. At the same time, China needs more policies and legislation to secure smooth direct financing channels and the stability of financing forms. The Chinese capital market is underdeveloped. At present, direct financing only accounts for a very small proportion of the country's entire financing. In the past few years, this proportion has sometimes fallen as low as 2-3%, and it will not exceed 10% this year. However, in developed market economies, even in Germany and Japan in which banks play a very important role, direct financing accounts for 30-40% of the total financing. In the USA, the proportion is as high as 60-70%. Banks should provide indirect financing and working capital. Funds for development, including those for ownership regrouping, should be provided via direct financing, including angel funds, VC, rounds of PE and pre-IPO investment. In short, China should vigorously develop its direct financing, including private funds.

Prof. FAN Gang is the president of CDI.

China Kicking Off New Forces of Economic Growth

Dr. ZhOU Junmin

In 2015, the GDP in China reached RMB 67.57 trillion, growing by 6.9% with a per capita GDP exceeding RMB 49,000. Although the GDP growth rate was low, it was still the medium rate in the history of GDP growth since the reform and opening-up of China, and the highest growth rate in the whole world.

The fall of the Chinese economic growth rate is intended to eliminate surplus capacity and debt and adjust the structure, thereby realizing the 'soft landing' of economic growth.

In the New Normal of the Chinese economy, the growth forces should shift into a stage characterized by more advanced forms, a more complex labor division and a more rational structure, so as to establish an economic growth model driven by innovation.

Emerging industries have become the new forces of economic growth. In 2015, the added value of high-tech industries rose by 10.2%, 4.1 percentage points higher than that of large-scale industries. Also in 2015, taxes from service industry accounted for 54.8% of the total, with the tax increment of the service industry taking up 80% of the total tax increments.

High-end consumption is another new force of economic growth. China has never lacked the need for high-tech and high-end services, and some requirements are in seriously short supply, e.g., high-tech intelligent automobiles, high-end intelligent mobiles, high-quality consumer goods, tourism and health services, medical services, education and business services, and so on. After this round of economic restructuring, enterprises will focus more deeply on developing original high-tech products and high-quality services.

We should increase public products and services and foster new forces of urban economic growth. By the end of 2015, the operating mileage of high-speed railways in China had reached 19,000 km, ranking No. 1 and accounting for over 60% of the total in the world. High-speed railways have generated evident network effects and greatly improved the business operation environment in China. The 49% household savings rate in the country provides sufficient funds for more public products and services. In addition, the PPP investment model has become a popular model for the new round of investments in China.

Dr. ZhOU Junmin is a research fellow at the Department of Urban and Industrial Economics, CDI.

Migrant Workers Becoming Citizens to Boost Chinese Economic Restructuring

Dr. ZHENG Xin

In 2015, the permanent urban population in China reached 770 million, with an urbanization rate standing at 56.1%. Urbanization is still an important driving force of economic growth. In 2015, the urbanization rate of the registered Chinese population was lower than 40%, indicating that the new-type urbanization featuring "citizen-oriented development" is still the driving force for sustainable economic growth in China.

This rapid economic growth can be attributed to industrialization and urbanization. Agricultural labor forces become migrant workers in cities and enter the high-productivity field from the low-productivity field. While increasing their incomes, they also help to boost economic growth. In 2015, the urbanization rate in China reached 56.1%, representing an increase of 1.33 percentage points over 2014. Additionally, China's GDP grew by 6.9%. If we presume that urbanization will be stable after the urbanization rate reaches 70-80%, we can expect that urbanization will generate 15-20 percentage points of economic growth.

When talking about the citizen-oriented development of migrant workers, we mean that they become genuine urban residents who have equal rights with the registered urban population.

This trend will increase the consumption of migrant workers in cities, which increases consumption expenditure, improves the consumption structure and better stimulates economic growth through consumption. In 2014, the monthly expenditure of Chinese farmers stood at RMB 944, less than one third of the monthly incomes of migrant workers. The citizen-oriented development of migrant workers will increase the consumption of migrant workers in cities and increase their demand for urban housing and high-quality products and services, thus providing further market demand for economic restructuring and upgrading.

In 2015, the urbanization rate of the registered Chinese population was lower than 40%. To ensure that the rate rises to 70-80%, more than 400 million farmers must become citizens. The citizen-oriented development of migrant workers will become a huge driving force for the economic restructuring and upgrading of China, the influence of which will be as big as when urbanization kicked off more than 30 years ago.

Dr. ZHENG Xin is a research fellow at the Department of Urbanization Research, CDI.

Projects >

On the Development Models and Experience of SEZs in China

Entrusted by the Ministry of Commerce of the People's Republic of China, the Institute has finished research into the "development models and experience of special economic zones in China" in November 2015. As an integral part of the country's top-level design, this research studies and summarizes the development models and experience of special economic parks in China in a systematic way, mainly concerning special economic zones, economic and technological development zones, high-tech development zones, special customs supervision zones and border economic cooperation zones. By reproducing and outputting this model, the Institute provides useful experience for the new round of China's 'going out' strategy.

Events >

The Shenzhen "Going East" Strategy Seminar

On November 18th, 2015, the Institute organized the Shenzhen "Going East" Strategy Seminar. Experts from the Central Government, Guangdong Province and Shenzhen discussed the topic of "Shenzhen going east, and the regional coordination and positioning of Pingshan". "Shenzhen Going East" is of vital importance for pushing forward the coordinated regional development of Guangdong.

Seminar on Building a High-Level Think Tank

In December 2015, the Institute was named among the pilot project of top 25 national high-level think tanks. On December 10th, 2015, the Institute hosted the Seminar on Building a High-Level Think Tank, which discussed "how high-level think tanks focus on developing major public policies urgently needed by the government" and "how high-level think tanks build more effective operation mechanisms".

Publication >

The "13th Five-Year Plan" and Long-Term Chinese Economic Growth

In 2015, the governments of all levels and all communities in China focused on compiling the 13th Five-Year Plans. This book is dedicated to reflecting upon the lessons and experience gained in making the past Five-Year Plans, discussing how to address development problems with global vision and strategic thinking so as to secure long-term stable economic growth in China, thereby guaranteeing that the new Five-Year Plan will play a better role in facilitating macro-regulation.

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