has accumulated a significant amount of capital, which will only lead to excess capacity if invested in the domestic market. Therefore, Chinese businesses should now compete in the world market and utilize global resources to seek new growth engines. China benefits from and advocates globalization, which will certainly continue to grow despite such setbacks as the rise of trade protectionism and short-term retreat.

New growth momentum

First, business environment. China's policies are increasingly pro-innovation and pro-entrepreneurship, with more tolerance of problems that might arise from innovation. For instance, the messy outcome of bike sharing is unimaginable in many countries, but is treated with tolerance in China. In China, new things get a chance to survive, and when there is a problem, supervision follows. In the next few years, a big share of China's growth will come from innovation and entrepreneurship.

Second, the development of financial systems, especially direct financing mechanisms. In the past, businesses took out loans from banks, but now they have more options, such as venture capital, PE, or selling equities. Finance plays a fundamental role in spurring innovation and entrepreneurship and the development of the financial system will come as an engine for economic growth in future.

Third, consumption growth. In the past, people born in the 1980s and 1990s used to be the main force of consumers, while retirees, who had little disposable income, spent very little. Things are different today. The wealthier generation begins to retire, and with both time and money, starts to consume more, transforming the country's consumption pattern.

Fourth, manufacturing development. The improved quality of some Chinese manufacturers will contribute to a stronger image of "made in China", instead of being a synonym for shoddy products. With improved consumer confidence in our products, the manufacturing sector will embrace a new round of growth.

Industrial development

First, that all industries have potential for growth does not mean all enterprises enjoy the same prospects, as they would experience constant mergers and restructuring. In the end, big enterprises will become even bigger and small enterprises will get merged into bigger ones. Enterprises shall fully consider how they would be merged so as to improve their production and innovation capacity. Research on the overcapacity in the steel industry in the American history suggests that the cause is vicious competition for resources among private enterprises during rail construction. Mergers and acquisitions are the destiny of many businesses. This is a good thing, as businesses can channel the return on investment into new undertakings.

Second, the manufacturing sector still has huge potential. In the 1980s, Korea was concerned about the industrial hollowing-out effect, worried that it would experience recession when industries move to China. However, the Korean economy has proved otherwise, gradually advancing to high-end growth. This rule also applies to China. We will be able to move forward as our manufacturing sector continues to climb the value chain.

Third, application of new technologies, and in particular, the internet. The internet is a public technology and serves every individual, company and industry, which makes it crucial for industries to keep pace with the information trend.

Fourth, professionalism and dedication. Successful companies are invariably those that are dedicated to their businesses and persevere for a long time, a quality that is indispensable in pursuing craftsmanship and an upgraded version of "made in China".

Fan Gang, President of CDI

Promoting BRI with Spirit of Reform and Opening Up

The implementation of BRI deepens China's reform and opening up and they are closely integrated with each other. In the course of reform and opening up that started since 1978, the most prominent feature is "Bringing In". The establishment of special economic zones, high-tech parks, bonded logistics parks, free trade zones and the introduction of capital and technology have directly driven the leapfrog development of China's economy and have also exerted significant impact on the world.

Under the context of the reform and opening up and with the advancement of BRI, the "Going Out" is endowed with new characteristics. First is the support of national strategies and policies. Second, we should focus on addressing top-level design issues such as policy coordination, infrastructure connectivity, trade, currency and people. Third, we should uphold the concept of shared development. Fourth, we should aim at sustainable development. Chinese enterprises should innovate and create a new model of Going Out.

Construction of overseas industrial parks is the highlight of BRI and has gained high recognition from countries along BRI. The construction of parks will not only drive local economic development and promote local employability, but also facilitate the transformation and upgrading of production capacity. Overseas industrial parks have become the strategic pillar of BRI and provided Chinese enterprises with a new platform of win-win cooperation.

In the new era, the implementation of BRI should be promoted with the spirit of reform and opening up. In this process, we should adhere to the concept of win-win cooperation, properly handle the relationship between "Going Out" and "Bringing In". That means China should export its own development experience and learn from others at the same time, which will greatly enrich the connotation of BRI. In addition, we should value sustainable development and share mutual benefits while implementing BRI.

Hu Zheng, Invited Researcher of CDI, Director of China Merchants Group, and Chief Representative of China Merchants Group in Central Asian and Baltic Region

Based in Shenzhen and founded in 1989, China Development Institute (CDI) is a non-governmental think tank that develops solutions to public policy challenges through broad-scope and in-depth research to help advance China's reform and opening-up. Based on rigorous research and objective analysis, CDI is committed to providing prospective, innovative and pragmatic reports for governments at different levels in China and corporations at home and abroad. In December 2015, CDI was designated as one of top 25 national leading think tanks in a pilot project of central government which is aimed at promoting the building of new-type think tanks with Chinese characteristics.

CDI Online
For more information, please visit our website:
http://en.cdi.org.cn/
Editor-in-chief: Carol Feng, Sophie Li
Email: carolf@cdi.org.cn, Sophieli@cdi.org.cn Tel/Fax: +86-755-8241 1011

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Belt and Road Initiative and China's Economy

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Pessimism Notwithstanding, Growth Picks Up

Growth was robust and stable throughout 2017, even as fixed asset investment and consumption kept weakening. Producer prices were elevated, while CPI showed little volatility. Monetary policy returned to moderately neutral levels, from its previous tight condition, and the money supply plunged .

External Accounts Are Balancing

Although China's stock market has been hit by the recent huge volatility in the U.S. markets, China's capital account seems to be shifting into balance. The outside market is volatile, but Chinese growth is strong.

Insights > more on page 03

Keeping Sober-Minded about China's Economy

"As an economist, I am very proud of achievements of China's economy. However, it is crucial to keep a realistic and sober amidst the chorus of praise. There will be something wrong if we do not address problems facing China's economy," said Prof. Fan Gang.

Promoting BRI with Spirit of Reform and Opening Up

The implementation of the Belt and Road Initiative (BRI) shall be closely combined with the reform and opening up, top-level design, shared development, sustainability. Construction of overseas industrial parks is the highlight of BRI. In the new era, the emphasis of BRI is to properly deal with the relationship between "Going Out" and "Bringing In".

Event >

South Pacific Night: Opening a New Chapter in Cooperation between China and Pacific Island Countries

On March 12, CDI held China-Africa Special Economic Zones Seminar in Coate d'Ivoire. Representatives from Ministry of Industry and Mines of Coate d'Ivoire, African Export-Import Bank, Agency of Management and Development of Industrial Infrastructure (AGEDI), Funds of Development of Industrial Infrastructure (FODI), Made in Africa Initiative, and Chinese enterprises in Coate d'Ivoire attended the seminar.

CDI experts brought up four reasons for success of Special Economic Zones in China. Firstly, the government actively guides to take full advantage of the role of market mechanism. Secondly, the industrial transfer opportunities have been seized to develop a comparative advantage. Thirdly, preferential policies are implemented to promote investment; and fourth, developers should clarify functional orientation, implement system engineering, and foster an excellent environment with high efficiency and low cost.

The construction of industrial parks can be divided into four stages: stage of investment, construction, management and operation. The investment stage should emphasize on development mode selection, development contents, fund raising and park legislation guarantee. During the construction stage, public and municipal facilities shall be promoted with considering how to combine with the post-stage operation. Three core tasks, including managing organization structure, institutional system and one-stop service center, need to be done during the management stage. Further, six operation platforms, business services, property management, investment consultation, financial services, human resources services and policy services shall be created during the operation stage.

Pessimism Notwithstanding, Growth Picks Up

Growth was robust and stable throughout 2017, even as fixed asset investment and consumption kept weakening. Exports rose, after two years of decline. Producer prices were elevated, while CPI showed little volatility. Monetary policy returned to moderately neutral levels, from its previous tight condition, and the money supply plunged.

GDP was up 6.9% for the year, and up 0.2 pps from 2016. Growth was consistent in quarterly terms, at 6.9% y/y in Q1 and Q2, and 6.8% y/y in Q3 and Q4. Value added for primary industry rose 3.9% in 2017, up 0.2 pps from 2016; manufacturing industry was up 6.1% y/y, flat on 2016; and services rose 8% y/y, up 0.2 pps. Industrial output rose 6.6% y/y, up 0.6 pps, though growth has been slowing. Fixed asset investment was up 7.2%, down 0.9 pps from 2016. After removing the price factor, investment was up 1.3% y/y, down 7.4 pps from 2016. Real estate sales turned from heating to cooling, the 19.5% y/y rise in Q1 falling to just 2.5% y/y by Q4, adding another factor in investment drop. Exports, conversely, picked up, rising 7.9% y/y, up 15.6 pps from 2016. Producer prices continued last year's appreciation trend. The ex-factory price of industrial goods rose 6.3% y/y, and PPI rose 8.1% y/y. CPI rose 1.6% y/y, down 0.4 pps from 2016. The main financial indicators experienced major decreases. By the end of 2017, M2 rose 8.2% y/y, down 3.1 pps from 2016; M1 rose 11.8% y/y, down 9.6 pps from 2016.

This year begins with intensive financial regulations. On January 5th and 6th, China's Bank Regulatory Commission issued three documents aimed at strengthening commercial bank regulation, related to trusted loans, bank equity and the too–big-to-fail mentality. These rules are responses to the central government's main goal, set at the end of 2017 for 2018, to contain financial risks. On December 20th, the central government listed alleviating financial risk as one of the top three tasks facing central government. This again is a continuation of the central committee meeting about financial risk in mid-2017, led by President Xi Jinping.

We view the potential financial risks in China as containable, as the regulators have recognized the problems, and are determined to take serious steps to deal with them. Shadow banking as part of financial liberalization requires prudential regulation. The Chinese government has the capability, and the advantage of designing regulation by absorbing the lessons of U.S. 2008 subprime mortgage crisis.

External Accounts Are Balancing

The ex-factory price index of industrial products was up 4.3% y/y in January, down 1.6 pps from Q4 2017. PPI was up 5.2% y/y, down 1.9 pps. Given tightening monetary policy, we expect producer prices will continue their downward trend in 2018. Due to the Spring Festival – the Chinese New Year -- many statistics are still

unavailable. We can only analyze data from imports and exports, and on financial conditions and price levels. CPI was up 1.5% y/y in January or 2% y/y after correcting for the Spring Festival factor, slightly higher than in Q4. Similarly, with tightening monetary policy, a CPI increase at this high rate of 2% is not sustainable. Trade growth is within normal range, after adjusting for the holiday factor. Imports were up 36.9% y/y. This very high growth rate was instantly adjusted for the holiday effect to 13.2% y/y, in a normal range instead. Exports were up 9.7% y/y after the holiday adjustment, up 0.5 pps from last December. The M1 money supply was up 15% y/y at the end of January. Considering that the holidays came late this year, the adjusted M1 growth rate was even lower than in December. The general declining trend has not changed. M2 money supply was up 8.6% y/y, lower than almost all months in 2017. RMB loans from financial institutions were up 13.2% y/y. Savings deposits from non-financial enterprises were up 12.1% y/y. These two relatively high growth rates were the main ones affected by the holiday. In January, the societal financing scale fell -17.2% y/y. In particular, the increase outside of RMB loans fell -74% y/y, with a share of only 12.1%. These are immediate outcomes of recent financial regulation tightening, and of de-leveraging efforts.

Although China's stock market has been hit by the recent huge volatility in the U.S. markets, China's capital account seems to be shifting into balance. All of China's external accounts turned to surplus in 2017, including the much worried-over FX reserve, adding $91.5 billion, from a $475.2 billion fall in 2016. The outside market is volatile, but Chinese growth is strong. The Chinese government is taking major steps to tackle any potential financial market disruption factors, as analyzed in detail in our recent reports. Based on these three factors, we expect in 2018 that the RMB-U.S. dollar exchange rate will be basically stable, that the capital account surplus will rise, and that foreign reserves will grow.

Insights >

Keeping Sober-Minded about China's Economy

Recently, especially since the beginning of 2018, public opinions in domestic and abroad have seen a great change from the previous decries to the current praises. The cover story in Time was titled "China won" and domestic opinion leaders also started to applaud the rise of China. It is however crucial to keep a realistic and sober mind amidst this chorus of praise.

Economic landscape and growth of China

China's economy went through a cycle in the 1990s, got over-heated from 1992 to 1994, experienced a five-year downturn from 1995 to 1999 and remained mired in a soft patch from 2000 to 2002 until finally recovering after the SARS outbreak in 2003. The second overheating came in 2005 and lasted till 2007. China went through a self-imposed restructuring as the world was hit by a financial crisis in 2008 and saw a periodic peak between 2009 and 2010 due to economic stimulus. Another downturn was experienced from 2011 onwards until

the economy touched the bottom in 2016 and started to warm up slightly in 2017; however, the economy was not bouncing back and would still stumble at the bottom for a while with certain unsolved issue.

In the short term, China's economy will maintain a 6.5-7% growth rate with a neutral macroeconomic policy without either stimulus or tightening, which will facilitate ongoing reform and restructuring before entering the next round of growth. It is thus important to see economic growth from a periodic point of view, and regard economic downturns as fluctuations. One thing that is worth noting is that it takes longer for China's economy to complete the process of soft landing than to restructure during crises. In the long term, we should be fully aware of the challenges facing China's economy, including rising labor and environmental cost, a widening income gap and a global landscape under newly emerged risks.

Potential is huge too, with per capita GDP at only 9000 US dollars, industrialization rate less than 70% and 30% of the labor force living primarily on agricultural income. Only 55% of Chinese people lives in cities and 70% of the population are low-income people, half of whom being farmers and half being migrant workers. Overall, China has low levels of consumption and high savings rate, with family consumption representing a mere 30% of the GDP. We shall have confidence in exploring this potential.

Changes in global landscape

External environment is a major source of uncertainties at present. Positively, developed countries have seen strong recovery driving China's exports. The Federal Reserve has raised interest rates and then China introduced a combination of policies by raising interest rate and lowering required reserve ratio, which remained neutral.

The "Trump effect" has indeed contributed to the rise of protectionism. What Trump does remind governments around the world of the need to reduce tax burdens on businesses, which is good. He deems that Chinese government has been correct in taking advantage of other countries for the interest of Chinese people, while the US government has failed to do so for the interest of its people, which is why he tries to make up for this gap. In future, he is likely to take measures in trade.

Does this mean a retreat of globalization? At first, globalization was advocated by developed countries. Their governments represented the interest of multinationals and domestic capital to promote globalization around the world. After realizing that globalization was against their interest, their domestic workers protested against this trend. However, at present, multinationals with global presence are still playing a crucial role in allocating resources worldwide as the drivers of globalization. A decade ago, developing countries had reservations about globalization, as they feared over the prospect of being dominated by multinationals and losing opportunities for job growth. Later on, however, as they found globalization actually contributed to their economy, they, including China, turned to be advocates of globalization.

China wishes to continue to attract foreign capital to gain know-how for its own development and many policies recently rolled out by the Chinese government encourage foreign capital to enter China by improving business environment. At the same time, China has also entered the stage of going global. High savings rate over the past two decades