imports rose 13.3% y/y, comparable to the rates of recent months.

CPI was up 2.1% y/y in July, up only 0.3 pps from the previous two months. In July, ex-factory production prices were up 4.6% y/y, down 0.1 pps from June. PPI rose 5.2% y/y, up 0.1 pps from June. Tightened monetary policy is on track to return to normal. At the end of July, the M2 money supply was up 8.5% y/y, and up 0.5 pps from June, and is possibly an indicator for an end to monetary policy tightening.

Currency fluctuation and financial risks have been frequently mentioned in the news headlines of late. Yuan depreciation, from 6.3 yuan per dollar at the beginning of this year to 6.87 on August 24th, has attracted a great deal of attention. Meanwhile, there have been reports of incidents of P2P lending bankruptcy, which even caused some investors to protest in their local financial districts. Of course,

these are potential risks to the economy and to the financial system in particular. But we believe the risks can be contained by China's sound fundamentals. Currency depreciation is strongly linked to an overall stronger dollar index, as seen from their strong correlation in our data graph. A Turkish lira-style collapse of the yuan is unlikely. We expect the yuan to fluctuate around 7 against the dollar this year. P2P lending is now under much tighter regulation and, given its relatively small size in the total financial market, is hardly anything likely to cause a systemic crisis.

## Surplus to the US Even Widened

Growth was stable but a bit lower in October. Industrial output was up 5.9% y/y, up only by 0.1 pps from September. Investment rose 8% y/y, having been rising for three consecutive months, and up 5 pps compared to the lowest rate in July. State investment is accelerated to counteract other negative growth factors.

Retail sales of consumer goods were up 8.6% y/y in nominal terms in October, down 0.4 pps from Q3, only up 0.1 pps from the lowest rate in May. Its real growth rate was 6.5% y/y, down 0.9 pps from Q3, reaching the lowest rate since this cycle of economic slowdown.


Despite of trade war, trade is booming. Exports rose 20.1% y/y, up 9.8 pps from Q3. Imports rose 26.3% y/y, up 7.3 pps from Q3. Trade surplus to the US widened in particular, possibly thanks to the strong dollar, reached 218.1 billion yuan in October, and rose 23.9% y/y.

Prices growth is expected to go downwards with the current non-loosened monetary policy. In October, CPI rose 2.5% y/y, same rate as September. The ex-factory price index of industrial outputs and PPI grew 3.3% and 4% y/y, down 0.3 and 0.2 pps from September respectively.

In the end of October, M2 was up 8% y/y, down 0.3 pps from September. M1 rose 2.7% y/y, down 1.3 pps from September, reaching new low since this downturn cycle, having already been lower than the bottom in last cycle in March 2015. However, the trend is still fast declining. Central bank has the incentive not to lower interest rate to keep RMB afloat.



Infrastructure investment growth rate had its first rise in October this year. In particular, it rose 3.7% y/y, up 0.4 pps from September. This has been shown in recent intensive announcements for new openings and approvals of mega-projects, such as speed railway. Chinese government's relative low public debt at 47.6% of GDP with its international peers made such investment possible and sustainable for a while. Stronger monitoring by central government over local government spending may improve infrastructure investment efficiency. The low central government debt also makes tax reduction possible, as it has announced on November 1st to reduce value added tax rate for private firms, SMEs, and high-tech companies. Both infrastructure investment and tax cut will generate future growth, and the former will have a boost to the economy even in a short term.

Insights >

## Private Enterprises Incorporated into SOE Operation Mechanism: an Unfavorable Trend

In recent years, state-owned enterprises have become less energetic. New regulations set up in the national anti-corruption campaign have put SOEs under more rigorous supervision, resulting in slower decision-making process and less capacity for risks. Thus the government shall consider how to further develop the private economy. The next round of economic growth needs to be underpinned by independent innovation, which inevitably comes with huge risks. Compared to SOEs, the private sector is energetic and more willing to take risks. A risk-taking spirit coupled with a good decision-making mechanism is prerequisites for fully realizing independent innovation and market flexibility to inject vigor into economic development.


Despite a lot of support given by the central government in legislation and policies to the private sector to protect their interest and create a more enabling business environment, the operation mechanisms of private enterprises are often incorporated into SOE management after their shares are acquired by state-owned capital. Although capital has remained unchanged in the short term, this practice represents an unfavorable trend in the long run as it undermines economic flexibility. To better utilize state-owned capital to serve the private sector, the preferred stocks are desirable as they allows SOEs to invest in private enterprises for profit without imposing their own management system on the latter. In this way, private enterprises can maintain their vigor while assuming risks by themselves.

*Fan Gang, President of CDI*

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



CDI
China Development Institute
NEWSLETTER
www.cdi.org.cn 2018 volume 5

CDI-NERI Macro Outlook >

### FDI Keeps Flowing In

Imports were up 19% y/y, up 8 pps from Q2. Trade also comprises a very small share of Chinese GDP, and we are still optimistic that H2 growth will be stable.

### Surplus to the US Even Widened

Growth was stable but a bit lower in October. Industrial output was up 5.9% y/y, up only by 0.1 pps from September. Investment rose 8% y/y, having been rising for three consecutive months, and up 5 pps compared to the lowest rate in July. State investment is accelerated to counteract other negative growth factors.

Insights >

### *Private Enterprises Incorporated into SOE Operation Mechanism: an Unfavorable Trend*

After acquiring the shares of private enterprises, large state-owned capital tends to operate private enterprises with SOE management mechanisms. This practice undermines economic flexibility.

News >

### CDI and CII to Promote China-India Healthcare Cooperation

In New Dehli, CDI and Confederation of Indian Industry (CII) co-organized a roundtable discussion on strengthening China-India cooperation in the healthcare sector on November 19. The participants ranging from policy makers, entrepreneurs to experts from China and India agreed that there is great potential for bilateral trade and investment in the healthcare sector and discussed how to facilitate the cooperation in the pharmaceuticals from the perspective of policy coordination. During the meeting, CDI and CII also signed a MOU according to which the two parties will further their cooperation in the joint research and events. The CDI delegation also participated in the 15th National Pharmaceutical Conclave 2018 and the 2nd National Biotechnology Conclave 2018.

In addition, the CDI delegation paid a visit to Sonata and Infosys in Bangalore to learn about India's information and technology industry on November 23.

Events >

# Belt and Road Summit: From Vision to Action

## Exploring New Visions for Asia-Europe Cooperation under "Belt and Road" Initiative

It is of great significance for Asian and European countries, as important players of the world economy, to seek new opportunities for cooperation for common development under the "Belt and Road" framework. In a bid to promote Asia-Europe pragmatic cooperation, China Development Institute and The European House – Ambrosetti jointly held a seminar themed "Belt and Road Summit: From Vision to Action" on November 22, 2018.

Under the "Belt and Road" framework, China and Europe shall enhance cooperation in infrastructure in Central Asia and Eastern Europe towards building an interconnected network linking the East and West for better connection between Asian and European economies. Meanwhile, Asia and Europe may explore possible models of aid for the industrialization of developing countries along the Belt and Road, such as helping them build local industrial parks and enabling connectivity with infrastructure facilities in the region to enhance their capacity for self-sustainable development.

*Fan Gang (President, China Development Institute)*

Europe and China shall fully capitalize on the BRI in exploring specific models for cooperation to create better connectivity for economic cooperation and trade and to deliver greater benefits to the people. At the same time, both sides shall support economic globalization and facilitate trade and investment against all forms of protectionism.

*Paolo Borzatta (Senior Partner, The European House – Ambrosetti)*

The Chinese chamber of commerce in Italy can serve as a bridge to engage Italian enterprises in projects in third markets such as the Mediterranean and Africa.

*Davide Cucino (Chairman, China Italy Chamber of Commerce)*




Italy and China shall foster an enabling environment of openness, inclusiveness and mutual benefit based on international rules and standards, deepen China-EU Comprehensive Strategic Partnership to deliver development dividends brought by greater Asia-Europe connectivity to all participating economies.

*Ettore Sequi (Italian Ambassador to China):*

China and other Asian and European countries along the Belt and Road shall continue to explore ways and measures for better coordination regarding development strategies and policy, jointly expand cooperation on investment and trade in emerging sectors; continue to enhance coordination of rules and innovation, put in place a dispute settlement mechanism as soon as possible, and facilitate Chinese standards to become international.

*Li Gang (Deputy President, Chinese Academy of International Trade and Economic Cooperation, Ministry of Commerce, P.R. China)*

The BRI has provided great opportunities for ASEAN countries in financing and industrial restructuring in the interest of creative industry transfer. In terms of trade facilitation, urgent issues that should be jointly addressed by China and ASEAN include customs cooperation regarding the exchange of information and mutual recognition of supervision, and other areas of bilateral and multilateral cooperation including market access, certification and accreditation, standards and measurement, and statistical information.

*Arham Abdul Rahman (Deputy CEO, Malaysian Investment Development Authority)*

European countries are of the general view that the BRI will have positive impact on promoting economic connectivity among Asian and European countries, but certain European countries remain skeptical of China's rise. To address this issue, China shall promote coordination of policy with European countries as it opens its economy wider. Both sides shall act in compliance with WTO rules and properly address disputes so as to make bigger the pie of common interest.

*Feng Zhongping (Vice President, China Institutes of Contemporary International Relations)*

The priority of the EU-China Bilateral Investment Treaty is market liberalization. Better market access will help provide a level playing field for European and Chinese companies. At the same time, both sides shall work together on the establishment of proper mechanisms for dispute settlement to protect the interest of European and Chinese enterprises.

*Claude Meyer (Senior Advisor, Center for Asian Studies, Institut français des relations internationales)*

China and other BRI countries may jointly build areas for economic cooperation and trade to forge synergy in attracting industries and production factors, and boost connectivity among central cities in the "Belt and Road" network to support regional economic development.

*Hu Zheng (Board Member and Vice President, China Merchants Group, CEO, China – Belarus Industrial Park)*



Italy is willing to boost cooperation with non-EU countries along the Belt and Road in the aviation sector, broaden air economic corridors linking Europe and Asia, promote supporting businesses such as passenger air routes, aircraft leasing, aviation finance, etc., and facilitate travelling and integrate tourism resources along the line to upgrade high-end service sectors.

*.Andrea Tucci (Vice President Aviation Business Development, SEA Group – Milan Airports)*

China shall enhance multi-sector cooperation with international organizations, further harmonize technical standards and improve rules for investment and financing in line with international standards to better support "hardware connectivity", i.e., infrastructure projects along the Belt and Road, as well as "software connectivity", i.e., people-to-people exchanges.

*Huang Ziheng (Vice President, Center for Financial Research & Development, China Development Bank)*

The model of "infrastructure facilities + industrial parks + cooperation on production capacity" shall be encouraged in forging Asia-Europe infrastructure connectivity, so that industrial parks will have better capacity to support the region through enhanced connectivity with surrounding infrastructure facilities. At the same time, an operation model that focuses on the full life cycle of industrial parks from investment to operation will help host countries industrialize.

*Shi Kun (Executive Director, Department of Regional Development and Planning, China Development Institute)*

The building of technology parks shall align with economic interests of host countries regarding industrial development and people's well-being. Shenzhen's international innovation village offers valuable experience for the sustainable development of overseas economic cooperation zones.

*Zheng Yujie (General Manager, Nanshan Yun Gu Innovative Industrial Park, China)*

CDI-NERI Macro Outlook >

# FDI Keeps Flowing In

Be related to financial deleveraging in both the state enterprise sector and in local governments.

Retail sales of consumer goods were up 6.5% y/y, down 0.8 pps from Q2. The previous housing boom might have crowded out consumption. Despite the U.S.-China trade war, total exports grew 6% y/y, up 2.7 pps from Q2. In particular, exports to the United States were up 6% y/y, up 2.7 pps from Q2, and showed no signs of declining. We expect exports to the United States, at least, won't decrease too much in future, given the currently weaker yuan. Adjusted